

Ms Patricia Faulkner AO, Mr Terry Mulder and Mr John Thwaites
Review of Electricity and Gas Retail Markets in Victoria
Department of Environment, Land, Water and Planning

By email: energymarket.review@delwp.vic.gov.au

21 April 2017

Dear Panel members,

Review of Electricity and Gas Retail Markets in Victoria ('the Review') - submissions made by Dr Ron Ben-David

I am writing to raise our industry's concerns over the recent personal submissions of the Chair of the Essential Services Commission of Victoria ('the ESC'), Dr Ron Ben-David, which were made to the Review together with a letter from him dated 28 February 2017 ('Submissions').

The Australian Energy Council ('the AEC') is the energy industry association representing 21 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia, and sell gas and electricity to over 10 million homes and businesses.

The AEC has already made a formal submission dated 28 February 2017 to the Review. This letter is supplementary to that AEC submission. The AEC is taking this unusual step, on behalf of its members, due to the unsubstantiated claims and inflammatory language contained in Dr Ben-David's Submissions.

The AEC does not believe it is appropriate for Dr Ben-David, as Chair of an independent regulator, to be making submissions to a review that are not the views of the ESC. At best, doing so is likely to confuse the audience. At worst, there is potential to undermine the all-important perception that the ESC is impartial and independent.

Dr Ben-David's Submissions

Dr Ben-David claims his Submissions represent a personal view only. This is not a credible assertion because:

- the subject matter of the Review (and his Submissions) go to the heart of the work the ESC is commissioned to undertake by the Victorian Government. Dr Ben-David's Submissions additionally make repeated references to both the ESC and challenges for energy market regulators, and contain recommendations to give the ESC more powers. We also note the repeated use of the word 'we', which presumably refers to Dr Ben-David and the ESC, throughout his Submissions.

- The Department's Review team has also posted Dr Ben-David's Submissions on its website under the title '*Dr Ron Ben-David, Essential Services Commission*'.
- We note that the Submissions are also now listed on the ESC website under its 'Research Papers' section, which is headed '*Research papers and submissions presented by and on behalf of the Essential Services Commission*'.

Given the important and central role played by the ESC (and its Chair) in the governance of energy markets in Victoria, it is important that its work is robust, impartial and credible, and is seen as such. It would have been entirely appropriate for the ESC to have made a submission to the Review. However, it is entirely inappropriate for the ESC's Chair to make personal comments in submissions to a public review, and publish them on the ESC website, which then represents them as being made on its behalf.

Specific assertions made in Dr Ben-David's Submissions

Dr Ben-David's Submissions make a number of serious assertions about the functioning of the retail electricity and gas markets, but do not adequately substantiate them.

Examples of these assertions include:

- ***Regulators and retailers alike have 'framed' their messages around a view that discounted prices are 'the norm' and that customers who pay more than these discounted prices only do so because they fail to shop around. This framing of the market may be encouraging customers to 'gamble' on the retail energy market by entering conditionally discounted contracts, rather than accepting less risky offers¹.***

A dictionary will define 'gambling' as to 'take risky action in the hope of a desired result'.

Why is a retail customer said to be gambling on a retailer's product if the terms of that product are clear? There is no gamble if the risk, for example, of not paying on time, then results in an increased bill in circumstances where that was a clearly stated part of the contract in the first place. Retailers are required by law to declare the conditions that apply to a price or a discount. These are rules based obligations, not probabilistic. There is no gamble.

With respect to Dr Ben-David's 'Pay to enter a conditional market contract'², this number has been arrived at by inferring a relationship between the average conditional and unconditional prices in the market. However, not every retailer offers both a conditional or unconditional product and therefore you cannot compare the average of the conditional with the unconditional products. Further, it is also not clear that these products are only differentiated by pay-on-time benefits—there may be other contractual elements that apply (such as direct debit, e-billing and solar).

The principle flaw with Dr Ben-David's argument is that it characterises unconditional discounted contracts that *some* retailers may offer as a 'usual price'. In fact, they are simply one of many contract types that are subject to various competitive pressures and pricing strategies. Once this is acknowledged it is apparent that the gambling metaphor is not analogous.

¹ '*Do discount wars benefit retail energy customers? Don't bet on it*', Dr R Ben-David, 28 February 2017 (pg14)

² Ibid (pg37)

Analogical reasoning can be a useful way to promote understanding, but disparate inferences such as these are unhelpful to reasoned discussion. These claims should be made using appropriate evidence and rigour, rather than a reliance on what the author considers to be intuitively the case.

- ***It is estimated that in 2015-16, 28.9 per cent of household electricity customers and 42.5 per cent of household gas customers were receiving the benefit of discounted prices***³

The AEC acknowledges that the commercially sensitive nature of retail pricing, along with competition law, creates an environment which makes it challenging for retailers to publicly share information concerning pricing approaches or strategies. This means that any market analysis on the basis of available market offers, discounts and customer numbers relies on a number of assumptions.

We note that Dr Ben-David has made statements about the proportion of customers receiving discounts. He refers back to the ESC's *Victorian Energy Market Report 2015-16* in doing this. A review of the report referenced does not identify the source of the quoted numbers. In any event, we note that the ESC only used information pertaining to a *subset* of all market offers in its report.

We caution the Panel in relying on Dr Ben-David's analysis on this matter: not only is the basis for the calculation unclear, but we suspect the assumptions made by Dr Ben-David are questionable⁴.

- ***Limited time offers***

Dr Ben-David also provides a case study, using his own household as the frame of reference⁵. Despite his acknowledgement that he understood the terms of the offer being made by his retailer, and failed to comply with them, he is concerned that the retailer's offer was no longer available to him when he did make contact with his retailer.

The making of offers available for a limited time, or upon certain conditions being met, is a normal feature of almost all markets we access in everyday life. In any case, to the extent that customers (or regulators) are concerned about conditional discounting or time-limited contracts, it is important to note that not all offers in the market at any given time have these characteristics. The diversity of tariff structures have demonstrably increased since the removal of price caps in 2009 - Origin Energy Ltd's 'Predictable Plan' (also known as the 'All you can eat' product) is a recent example of this diversity.

- ***Customer inertia***

Using himself as the frame of reference, Dr Ben-David goes on to express a concern that customer inertia is a direct result of retailers providing too much information, failing to communicate in a way that is designed to 'grab customers' attention' and requiring customers to contact them and engage with automated systems⁶.

However, the information retailers provide customers is largely driven by the legal and regulatory requirements regulators, such as the ESC, impose. The cumulative effect of a retailer's compliance

³ *'Do discount wars benefit retail energy customers? Don't bet on it'*, Dr R Ben-David, 28 February 2017 (pg29)

⁴ Dr Ben-David appears to have calculated the proportion of customers on a discounted product by using the following formula: $(\text{undiscounted conditional price} - \text{unconditional price}) / (\text{undiscounted conditional price} - \text{discounted conditional price})$. This formula assumes that retailers receive the same margin on conditional and unconditional products, therefore the proportions can be inferred based on the relative price differences. This is not true.

⁵ *'Do discount wars benefit retail energy customers? Don't bet on it'*, Dr R Ben-David, 28 February 2017 (pg18)

⁶ *Ibid* (pg 23)

obligations, plus a retailer's own customer service practices, can sometimes unavoidably result in a communications approach that does not enhance the customer experience.

Retailers also actively contact customers and proactively try to retain them in a competitive market. Churn is material to retailers because it costs money to have a diminishing customer base, and so retailers are incentivised to invest in customer retention.

Role of the ESC

Since the opening of the Victorian electricity market in 2002, the ESC has played an important role in ensuring the efficient and effective operation of the state's energy markets. In essence, the role of the ESC is to regulate the retail markets and provide timely, informed and considered perspectives on their operation so that consumers can have confidence that they are receiving an essential service reliably, affordably and sustainably.

The role of Chair of the ESC is a significant one. Like the chairs of other independent statutory bodies (Reserve Bank, Australian Energy Market Commission, Australian Energy Regulator) the public comments of these senior officials are given greater prominence than most individuals. By definition, their public statements reflect the intent of the organisation, and the veracity of their statements reflect its credibility.

We would observe that the Dr Ben-David's Submissions lack rigour and do not represent a robust and empirical analysis of the Victorian retail energy market. Given the significance of his role, the standard of this analysis invariably reflects on the ESC.

We welcome informed debate and discussion on the functioning of retail energy markets, and the Review has provided a useful forum in which that discussion can be held in Victoria. The AEC accepts that transparency and customer communication and engagement can always be improved and the industry is open to sensible discussions about retail market reform.

However, we do not support the Chair of the ESC using a government review to voice personal opinions, based on limited evidence and assumptions, in circumstances where an observer would assume that those representations were those of the ESC. The ESC itself must instead participate in genuine consultative processes aimed at assessing and improving retail energy markets.

We would be pleased to meet with each of you to discuss the industry's concerns. We request that this letter be published as supplementary to the AEC submission to the Review dated 28 February 2017 on the Department's website.

Should you have availability to meet with the AEC, please ask your Secretariat to contact Sarah McNamara in the AEC offices on 03 9205 3114 or sarah.mcnamara@energycouncil.com.au.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Matthew Warren', written in a cursive style.

Matthew Warren
Chief Executive