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Submitted via email [REDACTED]

16 December 2022

Review of Consumer Protections for Future Energy Services

The Australian Energy Council ('AEC') welcomes the opportunity to make a submission to the Australian Energy Regulator's ('AER') *Review of Consumer Protections for Future Energy Services* ('Options Paper').

The Australian Energy Council is the peak industry body for electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. AEC members generate and sell energy to over 10 million homes and businesses and are major investors in renewable energy generation. The AEC supports reaching net-zero by 2050 as well as a 55 per cent emissions reduction target by 2035 and is committed to delivering the energy transition for the benefit of consumers.

Australia's energy transition is hastening the creation and uptake of new energy technologies. These technologies represent a shift away from the traditional one-way flow of energy which the National Energy Customer Framework ('NECF') was designed to regulate. At the same time, the electricity that flows from new energy sources like small-scale batteries and solar panels maintain the same essentiality to the customer as electricity from a retailer, and this will only become more pronounced as the electricity system continues to decentralise.

The essentiality of new energy products and services is currently not captured in the NECF, meaning customers who use these new technologies are less protected. As uptake of these technologies grows, the absence of equal customer protections will create greater risks for customers. For this reason, the AEC submitted to the initial Issues Paper that the 'current regulatory framework is no longer fit for purpose' when it comes to protecting customers in a transitioning energy market. There are preferable regulatory models that can better incorporate the principles of competitive neutrality and essentiality.

The AER's Options Paper has taken a similar preliminary position: 'the status quo will not be fit for purpose for the future energy market and the need to regulate new products and services'. It has presented three reform pathways for stakeholders to consider.

While the AEC agrees with the AER's preliminary position, we are not convinced the three reform models put forward in the Options Paper adequately address the current and future problems with the NECF. These three options should instead be viewed as part of a spectrum of the types of regulatory models a regulator can take.

After assessing each option, the AEC proposes a blend of Option 1 and Option 2 ('Option 1.5') as the preferred regulatory model. Option 1.5 would see the AER pursue a more principles-based framework over time as the market for new energy services matures, but in the short term, extend some of the existing protections to non-traditional providers of an energy service. It is challenging while new products and services are in their relative infancy for a regulator, or even a market, to identify what a customer of that product or service needs to know when entering into an agreement.

While the AEC considers that a more principled approach will deliver better customer outcomes over time, in the short term this lack of clarity on customer needs will likely lead to ineffective principles, and the need for the AER to develop both principles and prescriptive regulation. This ultimately makes compliance more difficult and burdensome for regulated businesses.

Why is the NECF no longer fit for purpose?

The NECF was designed to regulate the one-way flow of electricity from the energy retailer to the customer. Electricity is an essential service so, as providers of an essential service, the regulations retailers face are comprehensive and strict. The regulatory burden this imposes is justified by the protections it provides to customers.

The emergence and uptake of consumer energy resources has created a gap in this framework. Customers are now accessing new forms of electricity supply like solar PVs and batteries to reduce their electricity bills and obtain some degree of self-sufficiency. But, these products and services, and their non-retailer providers, are not regulated through the NECF.

This is creating two major problems:

1. For customers, consumer energy resources are increasingly seen as an essential form of electricity, in particularly *affordable* electricity, but they are not regulated as if they were essential. This creates risks for the customer if suppliers create products and services that purport to offer a fungible alternative to grid supplied energy when in fact it does not.
2. For retailers, the absence of competitive neutrality reduces their ability to compete, innovate and ultimately provide new services for customers.

As uptake of consumer energy resources increases and the service models in which they are offered shifts from capital purchases to longer term contractual relationships, these problems will only grow, and so too the risks to customers. Any new framework then must ensure that the providers of an essential service are regulated and regulated equally.

AER reform models for consideration

Option 1 – Tiered authorisation

Tiered authorisation, as envisaged in the Options Paper, would see energy providers regulated based on how well they meet certain criteria. The AER's initial assessment sees traditional retailers as tier 1 entities (subject to the highest protection), while non-traditional providers are tier 5 (subject to a risk assessment). While this model is simplest to implement, the AEC does not believe adopting tiered authorisation will solve the challenges mentioned above in the longer term.

It places the bulk of the future regulatory burden on traditional energy retailers even though the transition will see customers source a greater proportion of their energy from non-traditional providers. In the AER's terms, this 'arguably creates regulatory inequality', and undercuts the principle of competitive neutrality among what should be seen as equal providers of an essential service.

Furthermore, it may result in more expensive outcomes for lower-income customers. It is known that lower-income customers are less able to access consumer energy resources, so are more dependent on a traditional energy provider. If these retailers are bearing all the regulatory costs, it will mean there is a higher cost to serve these customers.

It is also questionable whether tiered authorisation lays down an enduring framework for the regulator. The regulator will be required to undertake regular risk assessments of new energy products

and services. However, many of these products and services are currently unknown, making it hard to determine what their risks are. It seems probable in future that some tier 5 entities will be a significant source of a customer's electricity supply and treating them as the lowest authorisation tier will be seen as inadequate.

That said, this option is likely to deliver welcome and material improvements in consumer protections for customers in embedded networks.

Option 2 – Principles-based framework

The AEC considers a principles-based framework to have merit and should be capable of delivering an enduring and flexible framework that can react to new and unknown products and services. Right now, however, the option requires further detail, and the regulator needs to be confident that the principled obligations it places on businesses will deliver the outcomes they are seeking.

The challenge of a principled-based framework, and using the AER's recently published Better Bills guideline as a reference, is that regulators tend to supplement the principles with excessive prescriptions. The Options Paper seems to follow suit through its proposal that the AER provide guidelines on the interpretations of the principles. The AEC is cautious towards such guidelines because they invariably become a dictation, rather than a guide, for how industry must act.

While principles invite subjectivity through interpretation, this interpretation should be for industry, not for the regulator. Giving the regulator the power of interpretation through guidelines creates regulatory uncertainty as the regulations can change meaning on a whim. This is particularly detrimental to emerging industries.

The other difficulty is that a principles-based framework will require a major regulatory overhaul at a time when future products and services and their risks are not known. The AEC has concerns this will result in the principles being misdirected, and then overcorrected by more prescriptive regulation.

Option 3 – Outcomes-based framework

Industry sees an outcomes-based framework as the optimal model for regulators to aspire to. If done correctly, it gives industry participants room to innovate and regulators flexibility to adjust to the new, and unknown, products and services that will emerge through the energy transition. In theory, an outcomes-based model appears the most likely to set an enduring framework that does not require constant reform.

However, the AEC is not confident this model can be implemented effectively. The energy sector has previously attempted outcomes-based regulation and the experience is highly instructive of the types of challenges that will emerge. To use the example of hardship policy in the NECF, it was originally regulated through an outcomes-based model, where each retailer would submit to the regulator a tailored hardship policy that sought to meet the statutory objective. The regulator was able to approve or reject the policy based on whether the objective was likely to be met. This approach enabled innovation among retailers and different approaches to protecting customers.

But this also created inconsistencies across the policies, which made it difficult for the AER to regulate. The response was to introduce more and more minimum requirements into hardship policy regulation, to the point now where hardship policies have become standardized. Given the tendency of regulators to be conservative, this cycle seems destined to repeat itself.

The other challenge with this option is that introducing an outcomes-based model will require a complete overhaul of the existing NECF framework. This process will be long and costly, at a time when

the market is evolving rapidly. Above that, it will create inevitable friction about what the final framework should look like. Industry would fully expect that some critical retail responsibilities, like life support, would have prescriptive regulation.

However, the advantages of an outcomes-based model will be underdone when some stakeholders seek to have prescriptive rules in place for all retail functions. This process played out during the creation of the Better Bills guideline, where it was difficult to reach consensus on what bill information was “primary” (prescribed) and what was “supplementary” (optional).

Option 1.5

Given the problems outlined above, the AEC would encourage the AER to view its three reforms model as part of a spectrum, rather than the only three options open to consideration. Right now, the incomplete knowledge we all have of new products and services, and their future opportunities and risks, makes commitment to a complete regulatory overhaul difficult. At the same time, it is apparent the NECF does need modernising.

One suggested pathway is for the AER to gradually shift towards a principles-based framework over time as a better understanding of the future energy market emerges. In the meantime, the AER should focus on strengthening protections for customers using non-traditional products and services, similar to what it has done through its extension of NECF protections to customers in embedded networks.

Future responsibility for review

The problems and solutions outlined in this Option Paper involve important questions about the future regulatory framework for the energy retail sector. Given this importance, the AEC considers this review should eventually be transitioned to, and become the responsibility of, the AEMC, which is the designated energy rule making body. In the AEC’s experience, regulators are incentivised to create rules and regulations that are ultimately easy to enforce, rather than deliver positive outcomes for customers. The need for separation between the rule maker and enforcer is well-accepted and it should be no different here.

Any questions about this submission should be addressed to Rhys Thomas, by email [REDACTED] or mobile on [REDACTED]

Yours sincerely,

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