VICTORIAN

Energy Market

REPORT 2020-21

Easing the burden of unpaid bills

Actively enforcing the rules to build trust in the market

A ‘striking consumer preference’ for large energy retailers

ESSENTIAL SERVICES COMMISSION

An appropriate citation for this paper is:

Essential Services Commission 2021
Victorian energy market report: 2020–21
29 November

Designed by OÙ

This Victorian Energy Market Report meets our reporting obligations under Section 10AAB, 54V and 54W of the *Essential Services Commission Act 2001*, Section 39A of the *Electricity Industry Act 2000* and Section 47 of the *Gas Industry Act 2001*.

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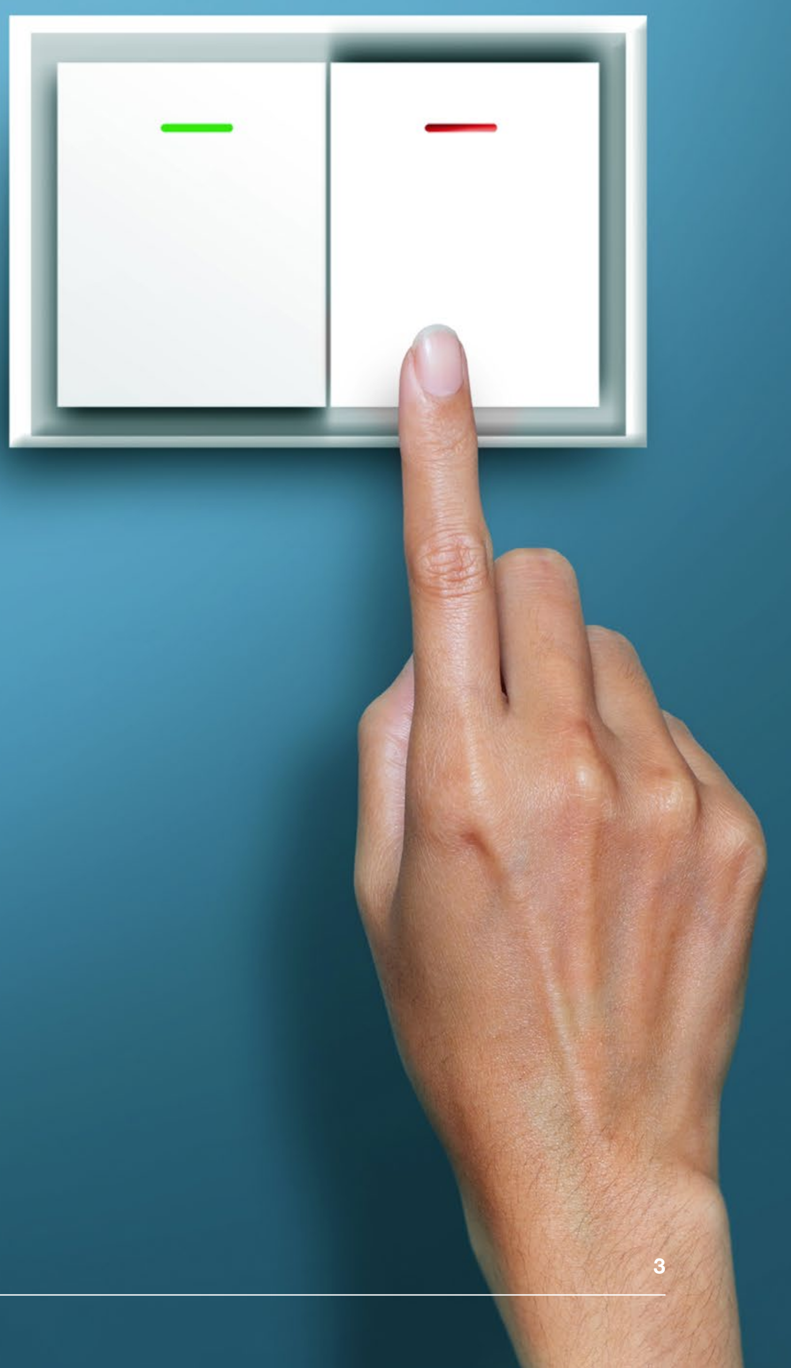


Chairperson's foreword

This is our sixth annual Victorian Energy Market Report. Our first was published in November 2016 with the aim of providing customers with information about the energy market that would promote effective competition… to achieve the best outcomes for energy consumers.

One of the key goals of this report has always been to build consumer understanding of how the market operates – and by doing so, empower customers to engage confidently to make choices that work for them.

This year our report looks a little different. Following the implementation of a new legislative function to monitor and report on the competitiveness and efficiency of Victorian energy markets we have refined our approach to reporting on the market.

We have redesigned the report to be more accessible to our readers, to pull back the curtain for consumers to help them take charge of their energy choices. You will see that this report consists of three articles giving insights into the performance of the market, and our role as the market's regulator.

The first article presents rigorous economic analysis and research we have undertaken to better understand customer preferences regarding their retailers. Our findings are clear. Victorian consumers still tend to prefer large energy retailers despite these retailers not always offering them the lowest prices in the market.

While this is not necessarily problematic, I do consider that this long-standing consumer preference is worth some attention. It suggests there may be opportunities to further build consumer confidence and trust to engage in the market as a whole, ensuring that the energy market delivers positive outcomes for consumers.

One way we work to build trust is by enforcing Victoria's energy rules. One of our key priorities over the past two years has been growing the commission's enforcement and compliance capacity, and preparing for legislative reform that is underway to modernise our regulatory toolkit.

Since 2018, energy businesses have paid more than $13 million in penalties for alleged breaches of the energy rules.

This includes $5 million in penalties that Origin Energy companies paid in October this year after allegedly charging prohibited exit fees to more than 20,000 gas and electricity small business customers. This is the strongest action we have taken against an energy company to date and shows how seriously we view behaviour that can undermine trust in the energy market.

The last article focuses on a third area of interest to many of our stakeholders including consumers, retailers, other regulators and governments. It relates to Victoria's payment difficulty framework – the strongest hardship framework for energy consumers anywhere in the country.

After almost three years since the framework was introduced in January 2019, the article's observations are being used in a review of its implementation. We recently shared these insights at a workshop with almost 90 industry and community representatives who shared their experience of the framework.

We hope you read our report with interest, and welcome feedback on our new approach and analysis. We look forward to continuing to monitor the performance and behaviour of energy businesses, reporting on the competitiveness of the market and working together with our stakeholders to promote the long-term interests of Victorian energy consumers.

Kate Symons
Chairperson

A ‘striking consumer preference’ for large energy retailers

When Victoria's energy market opened to full retail competition in the early-2000s, few predicted that nearly two decades later, 77 per cent of electricity customers and 85 per cent of gas customers in the state would still prefer a large retailer.[1,2]

This customer preference is both persistent and striking. To start with, while consumers state in surveys that price is the most important factor when switching, large energy retailer offers are generally more costly than those offered by small and medium retailers.[3]

What is a large retailer?

Energy retailers are categorised by their size (large, medium, or small) based on their share of each market; residential electricity, residential gas, small business electricity, and small business gas.

Despite presenting data and results by retailer size groups, it should be noted that each retailer size group has many individual retailers and median/average values do not always capture individual retailers' specific characteristics.

Size Group	Market Share per Licence	2020-21 Residential Electricity Retailer Size Groups
Small	≤ 1%	All retailers not categorised as medium or large
Medium	(1-5%)	• Alinta Energy • Dodo • Globird Energy • Momentum Energy • Powerdirect • Powershop • Sumo Power • Tango Energy
Large[4]	≥5%	• AGL • EnergyAustralia • Lumo Energy • Origin Energy • Red Energy • Simply Energy

In addition, most large retailer customers are not on their current retailer's 'best offer'. Despite facing more costly offers, large retailer customers are more loyal, with substantially higher customer retention rates than either small or medium retailers.

When customers do switch, most large retailer customers move to another large retailer, despite the lower prices offered by small and medium retailers. Why does this large retailer preference persist?

Pricing power and market power – what's the difference?

Pricing power is the ability for a provider or supplier to charge higher prices to a group of consumers.

They can do this because some consumers have relatively inflexible demand, which means that large price changes have relatively little impact on their consumption choices. Such demand can be caused by the essentiality of goods or services – such as petrol and electricity – or by specific physical or brand features that customers are particularly interested in.

Though market power includes the ability of a firm to set higher prices, there are several other factors to consider. This includes the ability to restrict competition, the ability to restrict other firms from entering the market, and behaviour that may harm consumers or competition more broadly.

Under Australian competition law it is not illegal to have or use market power. However, conduct by a firm with market power with the purpose, effect or likely effect of substantially lessening competition may contravene the Competition and Consumer Act 2010.[5]

1 Includes both residential and small business customers.

2 We thank Prof. David Byrne (University of Melbourne), Prof. Arthur Campbell (Monash University), Dr Gordon Leslie (Monash University), A/Prof. Leslie Martin (University of Melbourne), and other participants for their comments, input and insights when we presented our initial findings at a commission workshop in mid-2021.

3 The methodology for offer analyses uses financial year periods, unless otherwise stated.

4 AGL, Energy Australia, and Origin Energy were the incumbent energy retailers when Victoria opened to full retail energy competition. These three energy retailers currently have 55 per cent and 61 per cent of electricity and gas market customers, respectively.

5 Australian Competition and Consumer Commission (ACCC), Guidelines on misuse of market power, 2018, ACCC; *Competition and Consumer Act 2010* (section 46).

For their part, large retailers may not be concerned, as loyal customers might support higher prices and profits. This potential to exert pricing power is not necessarily due to a lack of viable competitors.

For example, Victoria's residential electricity market has welcomed many new electricity retailers over the last decade, pushing the market share of large retailers down.

Thus, some stakeholders have taken comfort from a decreasing Herfindahl-Hirschman index (HHI) as seen in Figure 1,[6] a market concentration measure where higher values suggest fewer competitors and lower values imply greater competition. However, as economists have pointed out since the 1960s, competition is not the sole driver of customer outcomes.[7]

It has been widely recognised that retail competition can be enhanced if customers actively search for better energy deals,[8] leading many regulators to add measures of customer engagement to their competition assessments.[9] The most common measure used is the number of customers switching retailers. However, the variability in customer switching rates is difficult to explain, and a customer's decision to switch retailer does not always lead to the lowest possible price.

For example, academic economists point to customer characteristics and preferences as substantial drivers of outcomes.[10] As well, energy customers may be risk-averse, or not have the time, patience or motivation to search for the best retail energy offer. Therefore, it may be logical that customers choose large retailers when balancing price, their own experiences of the market, convenience, and the perceived risk of choosing an unknown retailer.

Providing clear information about the actual risks and potential benefits of looking beyond large energy retailers could empower consumers. In fact, the Victorian retail energy market is governed by carefully crafted rules and regulations that ensure many of these perceived risks are minimised.

Since 2018, the rules have been further enhanced to regulate discounting practices and limit price changes to once a year. These changes have simplified customers' energy offer search, allowing them to compare prices more readily and focus on offer characteristics most important to them. Surveys tend to highlight price as the overall top priority,[11] but other offer or retailer characteristics might also be relevant.

At the same time, large retailers will be keen to keep their pricing power, as it can help maximise profits. This can be seen when looking at the price level of retailers' offers, where large retailers do not seem to be competing in the lowest priced market segments.

What is HHI?

The Herfindahl-Hirschman Index (HHI) is the most commonly used measure of market concentration. It is calculated by summing the squared market shares of all firms competing in a market.

A decrease in HHI over time indicates a decrease in market concentration and a more competitive market. HHI decreases both as the number of firms in a market increases and the disparity in size between those firms decreases.

If HHI equals 1 then the market is a monopoly, meaning consumers are supplied by a single seller.

6 Small business gas customers have faced a more concentrated retail market since 2016-17.

7 G Stigler, 'The economics of information', *Journal of Political Economy*, 1961, 69(3):213-225; J E Stiglitz, 'Equilibrium in product markets with imperfect information', *The American Economic Review*, 1979, 69(2):339-345; K Burdett, K Judd, 'Equilibrium price dispersion', *Econometrica*, 1983, 51(4):955-969.

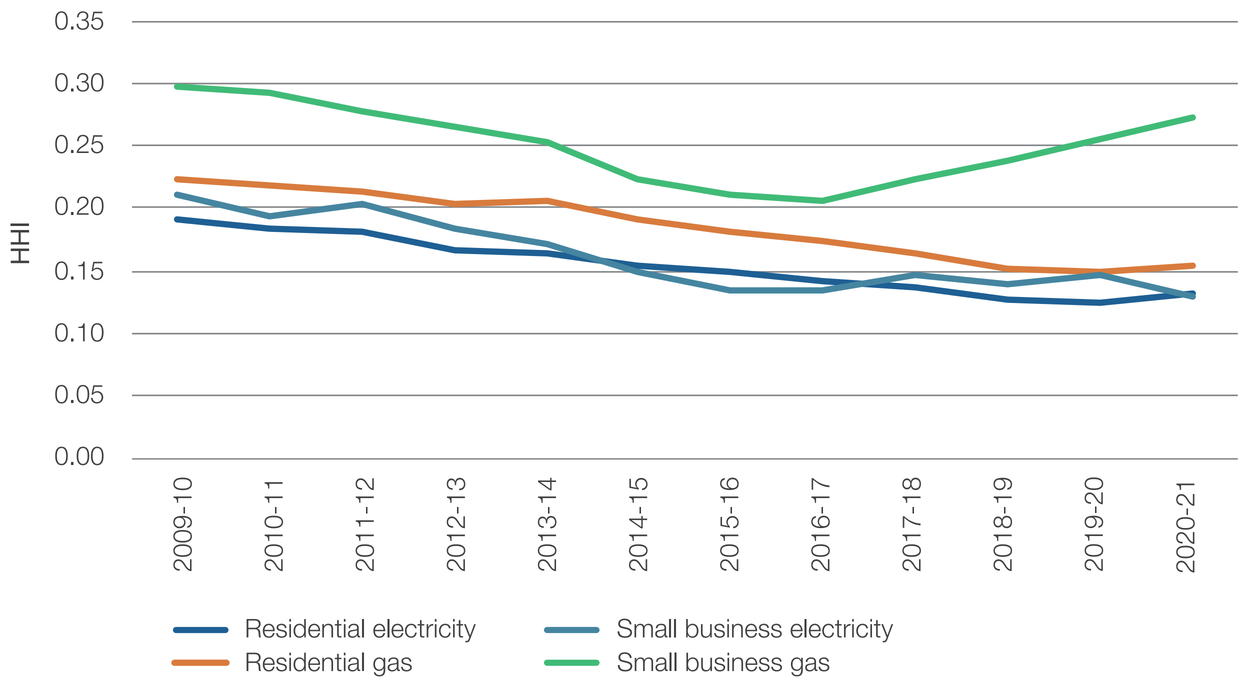
8 H Varian, 'A model of sales', *The American Economic Review* 1980, 70(4):651-659; S Salop, J Stiglitz, 'Bargains and ripoffs', The Review of Economic Studies, 1977, 44(3):493-510.

9 Australian Energy Regulator (AER), *State of the energy market report*, 2007-2021, AER; Australian Energy Market Commission (AEMC), *Retail energy competition review*, 2014-12020, AEMC.

10 Y Chen, T Zhang, 'Equilibrium price dispersion with heterogeneous searches', *International Journal of Industrial Organisation*, 2011, 29(6):645-654; D Stahl, 'Oligopolistic pricing with heterogeneous consumer search', *International Journal of Industrial Organisation*, 1996, 14(2):243-268.

11 For example, Energy Consumers Australia (ECA), *Sentiment Survey: June 2021* states that the main reason consumers considered switching retailers was "dissatisfaction with value for money".

Figure 1 – Victorian energy market HHI



What is a consumer preference?

Each customer values different things and values them differently. It is assumed that with a given set of preferences, a customer will desire a cheaper price.

However, this does not mean that customers always and only want lower prices. One customer may be willing to pay more than another customer because they value some part of an offer differently.

Large retailers: not always focusing on price

Since 2017, the median large retailer's offer has been consistently priced above the small and medium retailers median offer (see Figure 2).[12] For example, looking at the Jemena electricity distribution area in 2017-18,[13] the median large retailer residential electricity offer was about 10 per cent more costly than the median small retailer offer. This relative pricing difference continued into 2020-21, with large retailers' median offer still nine per cent higher than the equivalent small retailer offer.

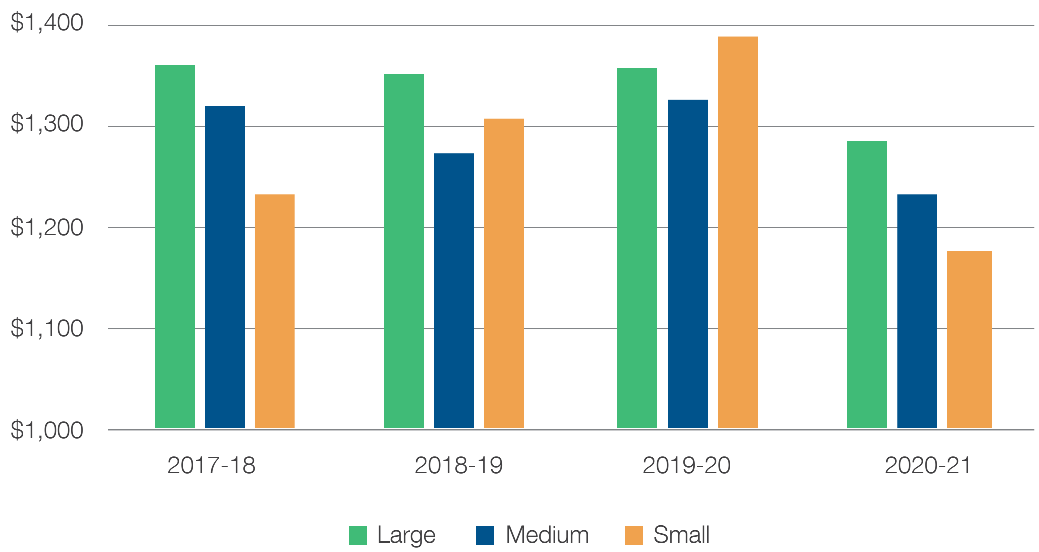
Similar pricing patterns appear in the Victorian gas market, as demonstrated by higher large retailers' median small business offers across all distribution areas in 2020-21.[14]

However, comparing median offers is only part of the story, as Victorian residential energy consumers benefit from a unique policy informing them if their electricity and gas retailer has a better offer available.

When looking at how many residential electricity and gas customers are not on their own retailer's best offer, evidence suggests that large retailers are again not necessarily competing on price alone, with the highest number of customers not signed to their retailer's best offer (see Figure 3 on the following page).

While the proportion of customers not on their retailer's best offer is high across the residential electricity and gas markets at 73 and 69 per cent, respectively – the upward trend in both residential electricity and gas markets is of greater concern. The intent of the best offer requirement was to 'nudge' residential customers toward cheaper offers and potential market engagement. It is likely that the coronavirus pandemic contributed to the observed trend by impacting customers' ability to engage in the market.[15]

Figure 2 – Victorian residential electricity median market offer by retailer group



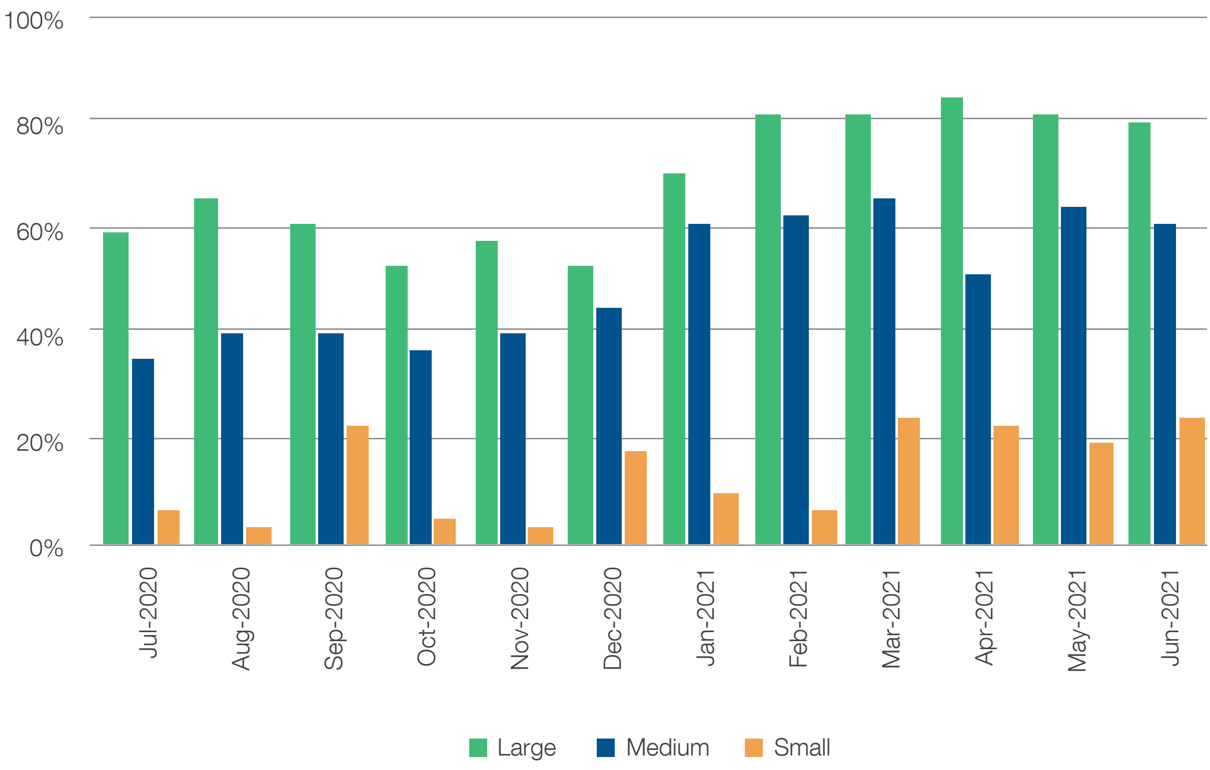
[12] The only instance where large retailers' median residential retail electricity offer was not above the other retailer groups was in 2019-20 when small retailers' median offer was highest.

[13] See 'Retailers and distribution businesses – what's the difference?'.

[14] Large retailers' median residential gas offers are the exception, as they are generally cheaper than the equivalent small and medium retailer residential gas offers. This exception is discussed as a potential reason for the large retailer preference in the "Bundling electricity and gas" subsection.

[15] Honeycomb, *Energy Market Insights,* 2021. Consumers are less concerned with their energy bills than other more urgent financial matters, which has likely resulted in less engagement.

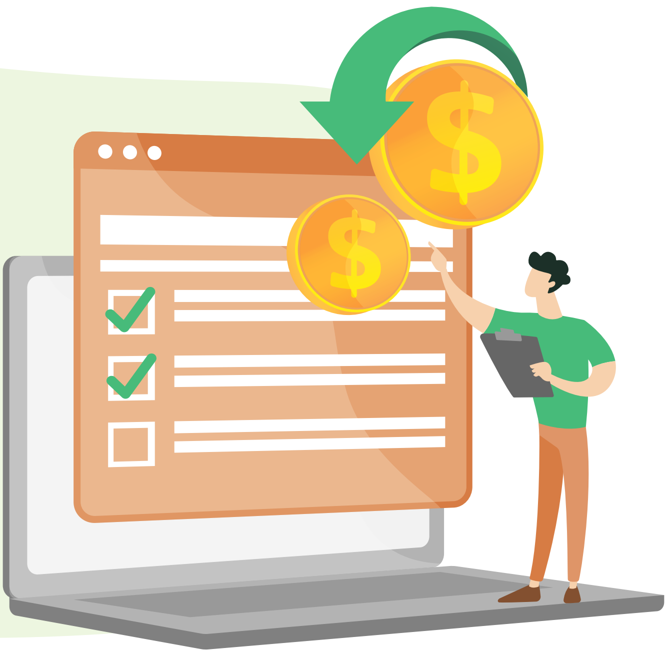
Figure 3 – Percent of Victorian residential electricity bills not on best offer by retailer group (2020-21)



What is a best offer?

Reforms that took effect as of 1 July 2019 mean that a retailer is required to inform each customer whether they are on the best offer with each bill.[16]

A retailer will determine whether a customer is on the best offer using that customer's past usage and comparing what they pay on their current offer against the cheapest generally available offer. Best offer reforms apply to both the electricity and gas markets.



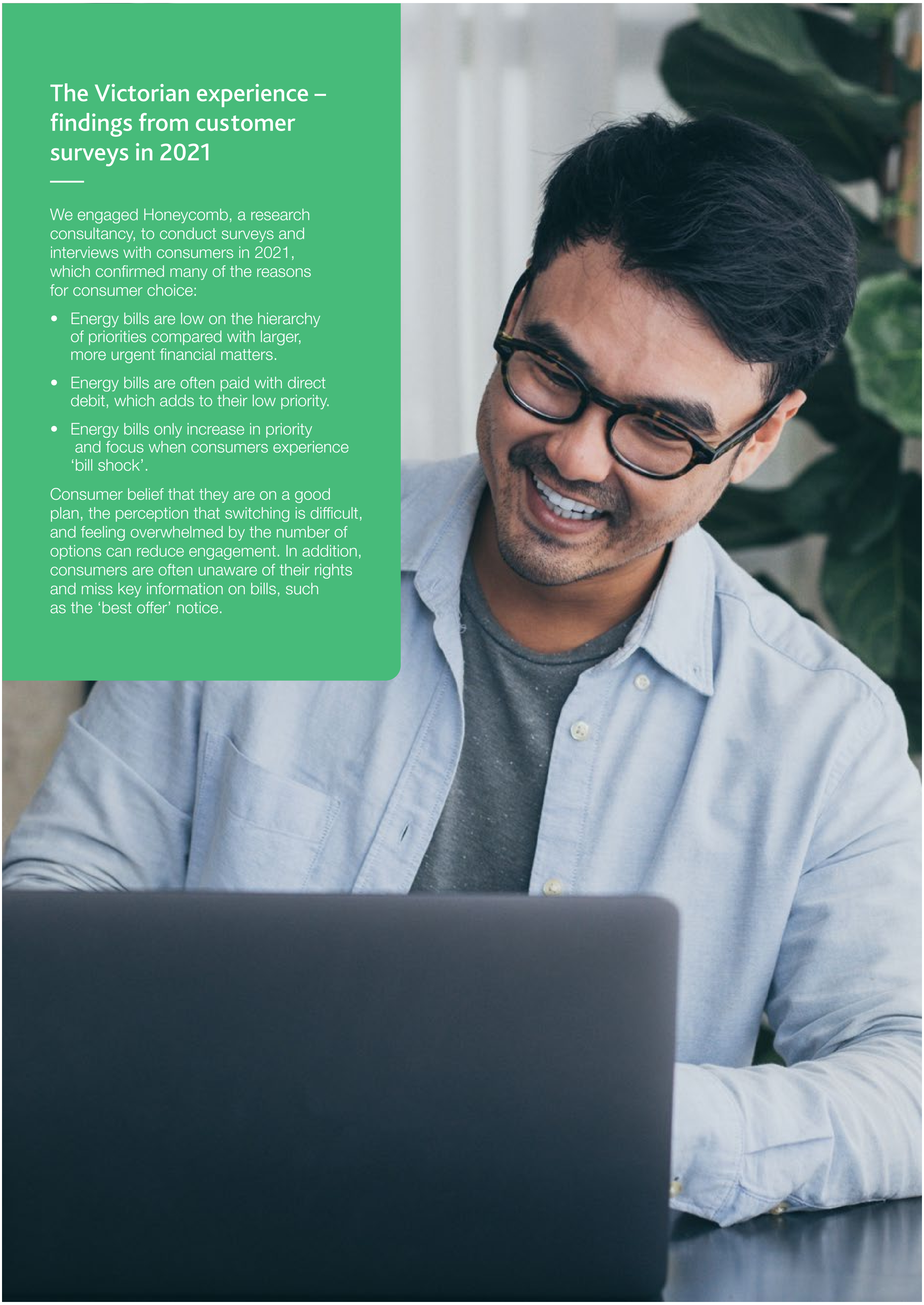
[16] For more detail on the methodology for calculating a retailer's best offer refer to Essential Services Commission (ESC), _Building trust through new customer entitlements in the retail energy market: Final Decision_, ESC, 2018, p 31.

The Victorian experience – findings from customer surveys in 2021

We engaged Honeycomb, a research consultancy, to conduct surveys and interviews with consumers in 2021, which confirmed many of the reasons for consumer choice:

- Energy bills are low on the hierarchy of priorities compared with larger, more urgent financial matters.
- Energy bills are often paid with direct debit, which adds to their low priority.
- Energy bills only increase in priority and focus when consumers experience 'bill shock'.

Consumer belief that they are on a good plan, the perception that switching is difficult, and feeling overwhelmed by the number of options can reduce engagement. In addition, consumers are often unaware of their rights and miss key information on bills, such as the 'best offer' notice.



Customers might be loyal to a fault

Retail residential electricity prices have been generally increasing since 2018 (see Figure 4), with increasing prices potentially incentivising customers to search for better offers. However, large energy retailer customers are additionally incentivised to search for better offers, as large retailers' offers are generally higher than their smaller competitors. Thus, it appears that customers of large retailers are very loyal. Such customers are sometimes referred to as 'sticky customers'.

First, large retailer residential customers are more likely to stay with their current retailer. This is clear when looking at customer retention rates over the past two financial years, where large retailers have kept more of their customers than either small or medium retailers (see Figure 5). Such retention rate differences are not trivial, with large retailers keeping a fifth more residential customers than the small retailer group in 2020-21.[18]

What is a 'sticky' customer?

Customer stickiness is the tendency of customers to return to a particular product or service. A sticky customer purchases a product or service more than once due to perceived value, whether it is pricing, convenience, product quality, or other transactional aspects. Increased customer stickiness can lead to higher customer retention.

Figure 4 – Victorian retail electricity prices paid, indexed (Victoria Energy Compare)[17]

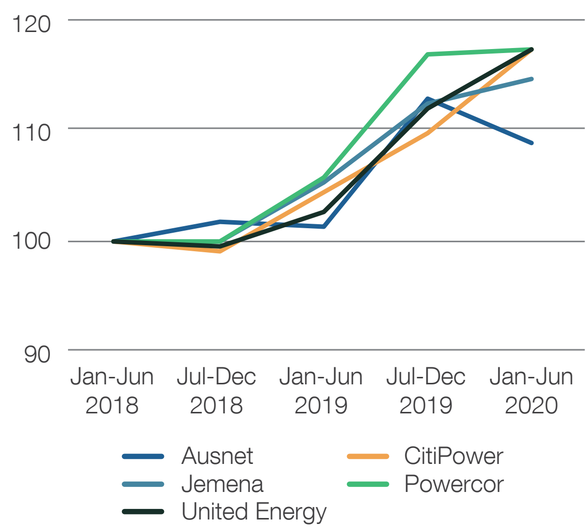
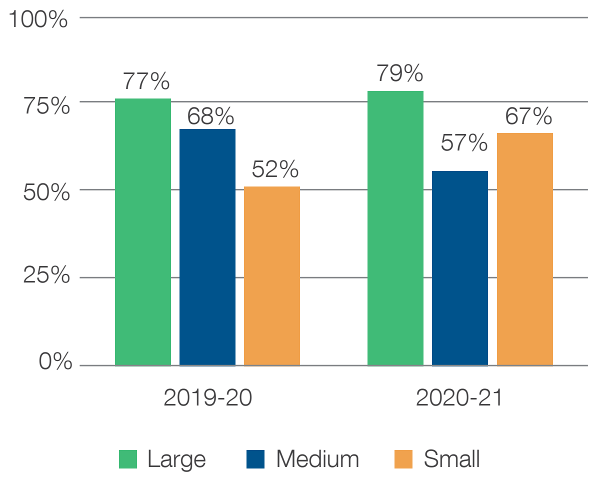


Figure 5 – Victorian residential electricity customer retention rate by retailer group



[17] The annual bill is calculated from a usage and a supply charge. It accounts for discounts, charges, solar rebates, and solar customer self-consumption. The calculation for an annual bill is: ('fixed charge per day' x 365 days) + 'usage charge per kWh' x (4,000 kWh - 'solar self-consumption in kWh') - 'total solar rebate'.

[18] Based on data collected from the commission's Compliance and Performance Reporting Guideline. This information is only available for residential customers.

Even when large retailer customers decide to switch their electricity retailer, most of these residential customers (60 per cent) sign up with another large retailer (see Figure 6). The proportion of customers moving to large retailers is similar for customers leaving small and medium retailers, at 56 and 63 per cent, respectively. In contrast, the small retailers, as a group, only win back 11 per cent of customers who decide to switch, with the medium sized retailers bringing back 25 per cent of their switching customers. As well, large retailers account for 96 per cent of new residential electricity connections, a high proportion even relative to their combined market share.

What is the customer retention rate?

The customer retention rate is the number of loyal customers at the end of the period as a proportion of total customers at the beginning of the period.

The number of loyal customers is the number of customers at the beginning of the period, minus the number of customers who transferred out.

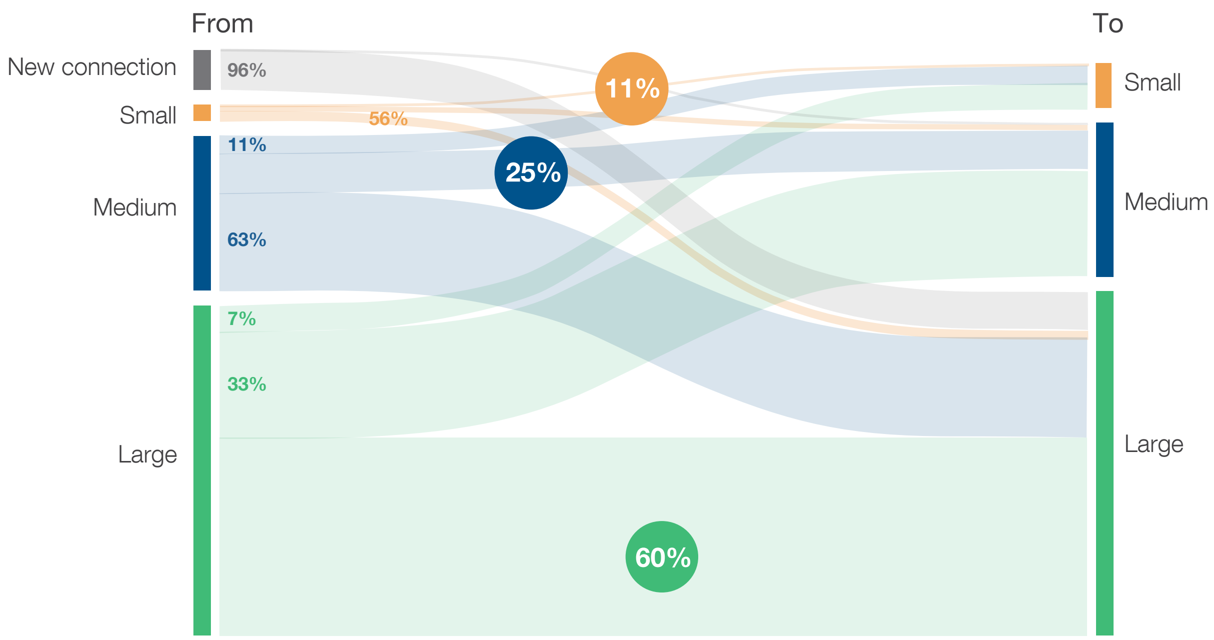
What do Victorian energy consumers think about searching the market?

We engaged U1 Group, a research consultancy, to gather and analyse the experiences of 40 Victorian consumers in searching for a new energy plan, using one or more comparison sites of their own choosing.

Most participants found the process of comparing different plans overly complex due to different billing structures, and felt overwhelmed by the number of options available. Several participants thought the perceived effort outweighed the reward.

Also, the cheapest plan was not always perceived as the best option, with participants indicating other factors, such as brand awareness, influenced their decision. Participants were more likely to choose a prominent retailer, with one participant commenting that, “[they] do like going with a company [they] know,” while another simply stated, “I want to go with a more known brand.”

Figure 6 – Victorian residential electricity transfers between retailer group (2020-21)



Potential explanations

There are several possible reasons for a large retailer preference. Some customers may incorrectly believe the lights will go out with a smaller retailer, also known as a supply risk. While supply risks are minimally impacted by the retailer, it is natural for customers to incorrectly link supply reliability and retailer choice (see 'Retailers and distribution businesses – what's the difference?').

However, there are other feasible explanations for a large retailer preference that require some deeper investigation, including:

- potentially better customer service quality offered by large retailers
- customers' individual experiences in the market
- the economies of scale and broader scope offered by large retailers for combined electricity and gas (and in some cases, telecommunications) contracts – a process known as 'bundling'
- the idea that customers may be attracted to – or only aware of – large or prominent retailers.

It should be noted that these potential explanations are neither exclusive nor exhaustive.

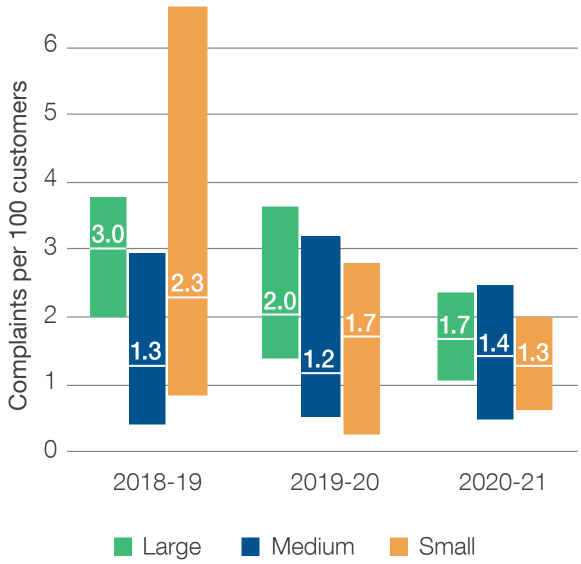
Customer service quality

Assessing if customers expect better customer service quality from large retailers is not necessarily a straightforward process. While customer service quality is difficult to measure, customer complaints are easier to count and can serve as a service quality proxy, where lower customer complaints might point to better customer service.[19] However, the picture is complex.

Figure 7 shows the median and standard deviation of residential complaints. When measured by complaints per 100 customers, at first glance it appears that large retailers' customer service quality is not always better than the service quality at small and medium retailers. In fact, median per customer complaints are higher for large retailers than either the small or medium retailer group for the three years considered.

However, closer inspection shows a clear difference in the variance of complaints between retailer groups, meaning that there may be more certainty around the level of customer service at a large retailer than with medium or small retailers.

Figure 7 – Victorian residential electricity customer complaints per 100 customers (median and standard deviation)

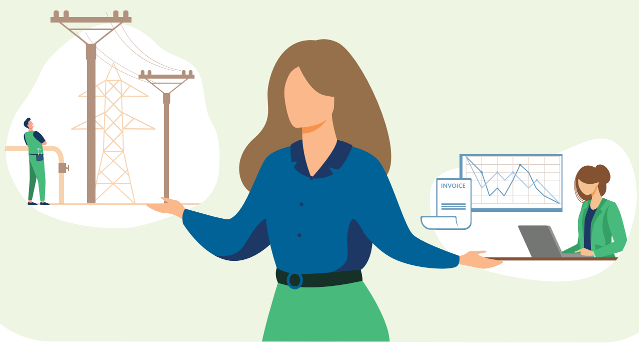


Retailers and distribution businesses – what's the difference?

Retailers and distribution businesses play different roles in getting energy to the end user.

Distribution businesses transport energy to different suburbs by delivering electricity through poles and wires, and gas through pipes. They are also in charge of building, maintaining and operating the distribution networks to ensure the reliability of supply. The five distribution businesses that service Victoria are AusNet Services, Jemena, Powercor, CitiPower, and United Energy. Each business is responsible for servicing a discrete distribution area.

Retailers buy the energy from the wholesale market and coordinate its supply to consumers. This includes issuing energy bills to customers.



19 Consumer performance reporting guidelines (CPRG), retailer self-reported complaints.

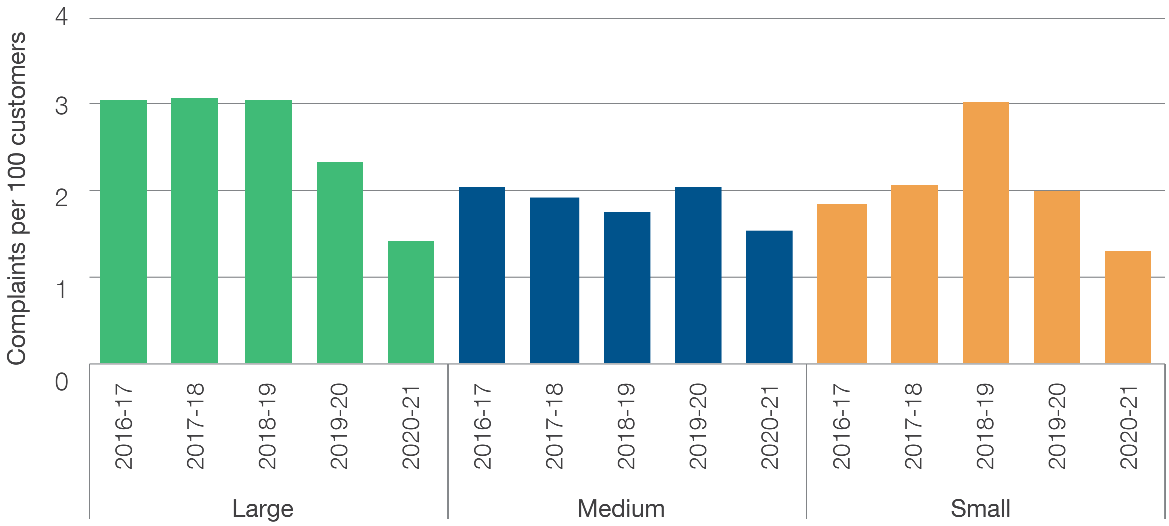
Therefore, it is possible that customers are particularly sensitive to a *potential* negative customer service experience and prefer the greater certainty that large retailers may provide. Alternatively, it may be that a small proportion of small and medium retailer customers who actually receive poor service quality, switch to the perceived certainty of better service quality from large retailers.

Further supporting the idea of customer risk aversion concerning customer service quality, Figure 8 shows that large retailers have reduced the number of complaints per customer over the past five years. For customers of small and medium retailers, complaints per customer have also been decreasing over the five-year period, but with a less consistent downward trend.

However, there are several issues with the idea that customer service quality expectations alone can explain customers' preference for large retailers:

- Customer complaints data is complicated for both electricity and gas markets, with a larger variance in customer complaints for large retailers in some years.
- Customer complaints might not be customers' preferred measure of customer service quality.
- It is unclear if customers can see real differences in customer service quality, as they may rely more on word-of-mouth or their own individual experiences.[20]
- While surveys typically place service quality amongst the top customer concerns, customers almost always rank price as their first priority.[21]

Figure 8 – Victorian residential electricity complaints per 100 customers



[20] U1 Group, *Customer Experience Research Report*, 2020, highlights some survey participant's preference for an energy retailer that has been around for longer and one they are familiar with.

[21] U1 Group, *Customer Experience Research Report*, 2020, found that price was the primary interest for survey participants when comparing offers, with retailer reputation and customer service expectations as the second and third rank considerations, respectively.

Customers' experience

Although energy customers typically rank price as their first priority, there is some evidence that customers' retail energy market experiences partially drive their preference for large retailers.

Small and medium residential electricity customers who switch overwhelmingly move to large retailers, with nearly three-fifths of customers who leave their small retailer choosing a large retailer. The equivalent number is even higher for those customers previously with a medium retailer, with over three-fifths of these customers selecting a larger retailer.

Such a clear preference for large retailers, even when customers were previously contracting with a small or medium retailer, is an example of a revealed preference.

Revealed preferences are often not explicitly stated preferences, but are instead 'revealed' by customers' market decisions. In this case, while price is explicitly ranked as customers' top priority, there are other non-price factors leading customers to prefer more expensive offers from large retailers.

Investigating further, two reasons for this large retailer revealed preference are explored; revisiting customer service quality, and customer experiences from the early days of energy retail competition.

First, customer service is an idea that captures multiple customer experience dimensions, including:

- ease of contracting (for example, signing up, contract transparency)
- billing clarity
- communication
- resolving issues in a timely and fair manner.

Virtually all aspects of a customer's experience, except price, can be defined as customer service. However as previously discussed, many of these customer experience dimensions are not potentially captured in customer complaints data. Customer service expectations might be set based on individual experience more than looking at customer complaints data.

Given the clear revealed preference for large retailers, the logical conclusion is that small and medium retailers may provide a less attractive customer experience when compared to large retailers.

Second, some customers did not have positive experiences in the early days of retail energy competition, which might continue to influence their views of energy retailers. This can be viewed as an informed risk aversion to less well-known retailers, resulting in some customers avoiding them, despite the potential savings.

In 2017, an independent review was conducted into the Victorian electricity and gas retail markets to identify whether they were operating in the interests of consumers.[22] The review found that these markets were not necessarily working as competitive markets. It also found that energy retailers with lower expected costs were charging consumers at the top of the price range, the additional costs of introducing competition in the market were being passed on to consumers, and discounting practices were being used to hide higher retail fixed charges.

What is a revealed preference?

'Revealed preference' is the term economists use to describe the action individuals actually take. It stands in contrast to stated preferences, which describe what a consumer says they will do.

The term 'talk is cheap' is often used to describe stated preference, because it can be common for people to say one thing and do another. Revealed preference is meaningful because it provides an objective way to measure something difficult to quantify – the subjective value a consumer places on a good or service.

It is difficult to compare how much one customer values customer service, as opposed to another customer's value of convenience. When consumers transact in the market, they are revealing these subjective decisions. Revealed preference theory emerged as a tool to help economists understand consumer choice.

22 J Thwaites, P Faulkner, T Mulder, *Independent review into the electricity and gas retail markets in Victoria*, report to the Victorian government, 2017.

Convenience: Paper bills

One potential benefit for large retailer customers is that all large retailers can send a paper bill in the post, which can then be easily paid at post offices or banking locations.

Customers who prefer these options are generally older and more likely to interact with their energy retailer directly, either via telephone or postal correspondence. While all large retailers can send paper bills, some small and medium retailers only provide bills via email. This may create uncertainty for some customers who then default to a large retailer, as a paper bill might be a requirement for them.

Convenience: Bundling

The retail gas market offers another possible explanation for the observed large energy retailer preference, particularly when considering customers who combine their electricity and gas contracts under one retailer. This 'bundling' of services may appeal to customers because large retailers' residential gas offers are amongst the cheapest.

Therefore, if customers prefer the simplicity of a single retailer supplying both their electricity and gas, it might be cheaper overall to sign up with a large retailer whose relatively expensive electricity offer is offset by a relatively cheap gas offer. The argument is that large retailers provide cheap and convenient energy services when customers bundle their electricity and gas contracts with a single large retailer. However, bundling services with a large retailer is not necessarily more convenient or providing the cheapest price.

First, even if customers contract both their electricity and gas services through a single retailer, they may continue to receive two separate bills. This is effectively the same experience for customers contracting their electricity and gas services through separate retailers.

Second, customers searching for the lowest priced offers can contract their electricity and gas services through the cheapest options available, even if via separate retailers. Given that large retailers are generally not offering the cheapest electricity prices, customers who bundle cannot achieve the cheapest overall energy price. Though some customers are convinced by the simplicity of choosing a large retailer for both their electricity and gas services, the outcomes do not align with surveys highlighting customers' substantial preference for cheaper prices over all other factors, including convenience.[23]

Prominence and incumbency

Even in extremely competitive markets, economists have come to understand that the time and effort required to search the market is one of the main drivers of persistent price differences, particularly when the benefits are unclear.[24]

Economists have developed explanations linking the difficulty in engaging with the market with choosing a large (prominent) brand. For example, markets with complex pricing can lead to consumer confusion, and confused consumers tend to favour prominent brands.[25] For many energy consumers, searching for and evaluating a new offer can be very complicated, as found in our recent consumer experience research.[26]

Another explanation is that the prominence of an option influences the likelihood a consumer will consider it first.[27] Prominence can take many forms, such as the first result when searching online, purchasing a product positioned at eye-level on a store shelf, the use of brand awareness advertising, or being the only brand a consumer is aware of.

Whatever form prominence takes, the main goal is to influence customer decisions. Incumbent retailers in Victoria have the benefit of large customer bases and a long period of operation, so to many customers, these are the only energy brands they know. To firms, increased prominence can positively impact profits.[28]

23 U1 Group, *Customer Experience Research Report*, 2020

24 G Stigler, 'The economics of information', *Journal of Political Economy*, 1961, 69(3):213-225; P Diamond, 'A model of price adjustment', *Journal of Economic Theory*, 1971, 3(2):156-168; J Reinganum, 'A simple model of equilibrium price dispersion', *Journal of Political Economy*, 1979, 87(4):851-858.

25 I Chioveanu, 'Prominence, complexity, and pricing', *International Journal of Industrial Organization*, 2019, 63(March):551-582

26 U1 Group, *Customer Experience Research Report*, 2020

27 M Armstrong, J Vickers, J Zhou, 'Prominence and consumer search', *The RAND Journal of Economics*, 2009, 40(2):209-233.

28 A Rhodes, 'Can prominence matter even in an almost frictionless market?', *Economic Journal*, 2011, 121(566):297-308.

Profits

Although the market share of large retailers has declined over time, they have captured a sizeable and consistent customer base in both the electricity and gas markets. In the residential electricity market alone, large retailers are virtually guaranteed 2.1 million customers annually (see Figure 9), with similarly high customer numbers in the retail gas market.[29] At the same time, large retailers have generally maintained a stronger financial position compared to their small and medium competition.

Although actual earnings before interest, taxes, depreciation, and amortisation (EBITDA) margin levels cannot be reported due to commercial sensitivities, Figure 10 shows that large retailers have generally outperformed small and medium retailers in the Victorian energy market.

Comparing median EBITDA margins, large retailers achieved higher margins than medium retailers by 15 percent in 2018-19. Nevertheless, as margins are a function of several factors, higher EBITDA margins alone are not evidence of pricing power. Such high margins might be driven by cost efficiencies. In fact, on average, large retailers' reported operating costs were the lowest of all retailer groups in 2019-20. However, with lower average retail operating costs and the cost efficiencies that come with scale,[30] it is notable that large retailers are not offering the lowest prices in the market.

Figure 9 – Residential retail electricity customer count by retailer group

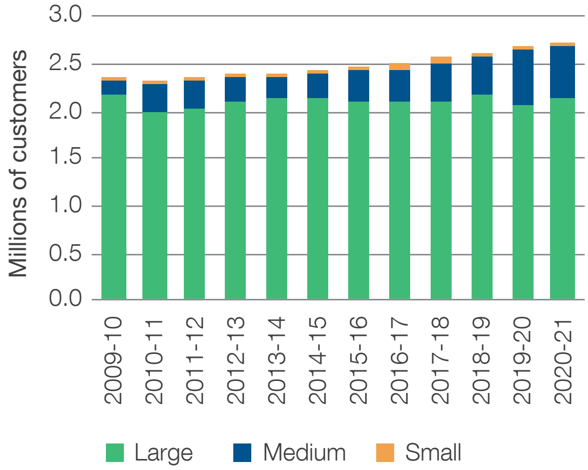
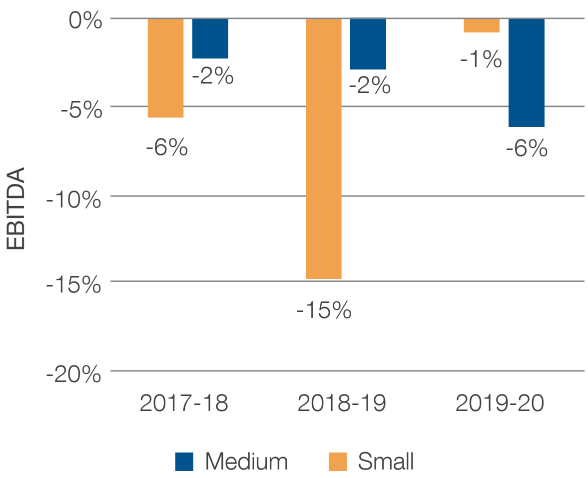


Figure 10 – EBITDA difference between large and small/medium Victorian energy retailers[31]



What is EBITDA?

EBITDA is an abbreviation for earnings before interest, taxes, depreciation, and amortisation.

EBITDA is a good measure of the overall financial performance of a company because it removes the effects of financing and the costs of capital, allowing comparisons to be made across companies and industries.

29 Large retailers have a customer base of 1.8 million in the residential gas market.
30 Based on data collected as part of the VDO cost data request to Victorian electricity retailers.
31 Reporting specific EBITDA values for retailer groups could directly or indirectly include commercially sensitive information.

The price distribution of residential electricity offers is shown in Figure 11 for the Jemena distribution area, which is further decomposed by retailer size groups in Figures 12-14. Comparing these figures shows how small, medium, and large retailers have priced their offers relative to each other.

Small and medium retailers sell offers across the market, from the cheapest to the relatively expensive. In contrast, large retailers firmly focus on middle-to-high priced offers.

Figure 11 – Distribution of residential electricity market offers by retailer group (2020-21, Jemena)

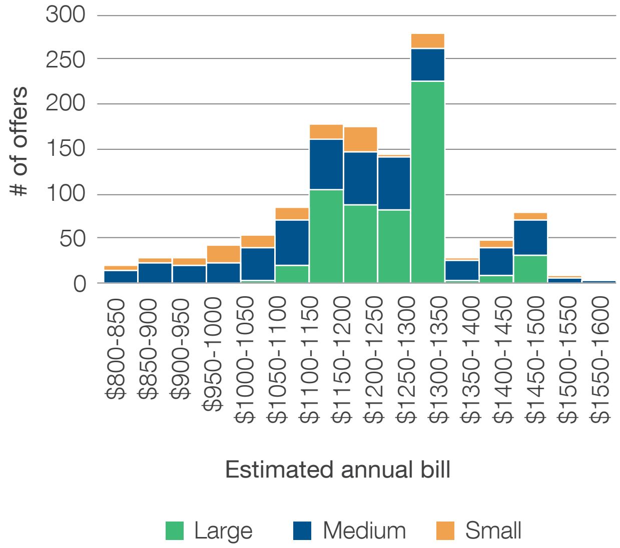


Figure 12 – Distribution of small retailers' residential electricity market offers (2020-21, Jemena)

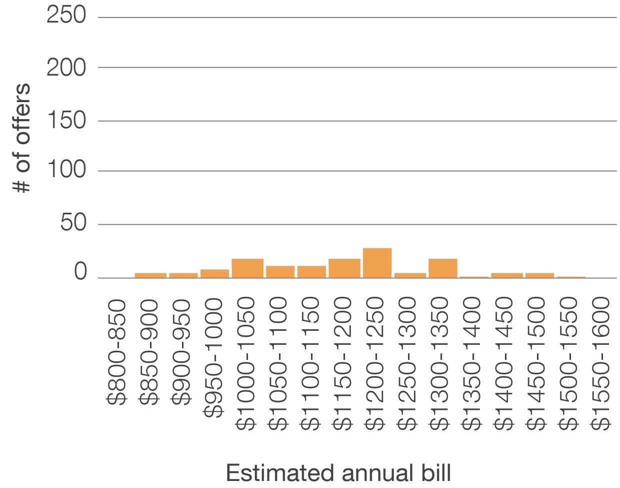


Figure 13 – Distribution of medium retailers' residential electricity market offers (2020-21, Jemena)

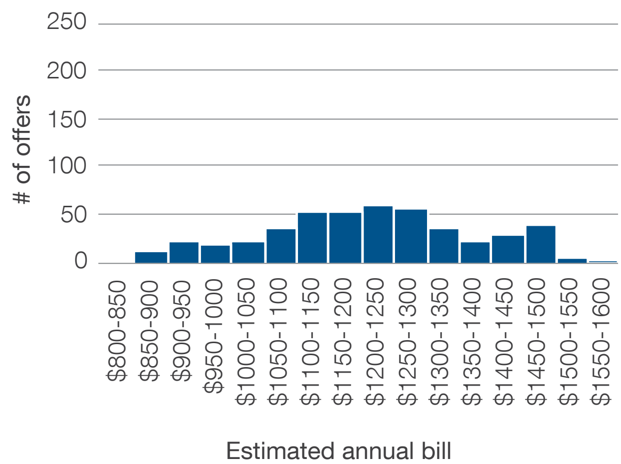
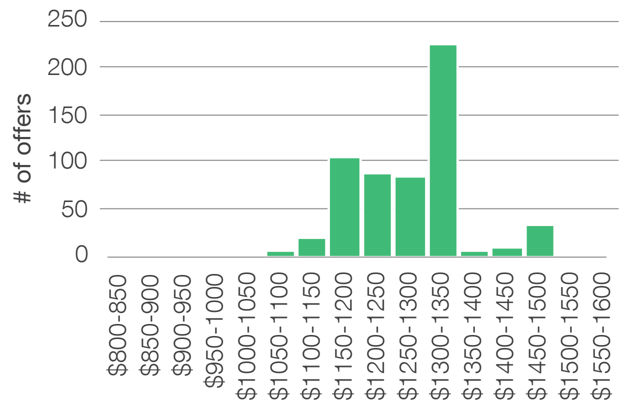


Figure 14 – Distribution of large retailers' residential electricity market offers (2020-21, Jemena)



Figures 15-17 further explore retailer strategies by looking at over-time trends in the residential electricity market for the Jemena distribution area. The median offer price trend is complex, but only large retailers have increased their offer prices between 2016-17 and 2020-21.

At the same time, only large retailers have decreased the standard deviation of their offer prices between 2016-17 and 2020-21. All of this means that large retailers have held their offer prices in the middle-to-high ranges in the market.

Figure 15 – Median and standard deviation of small retailers' residential electricity market offers (2016-17 to 2020-21, Jemena)

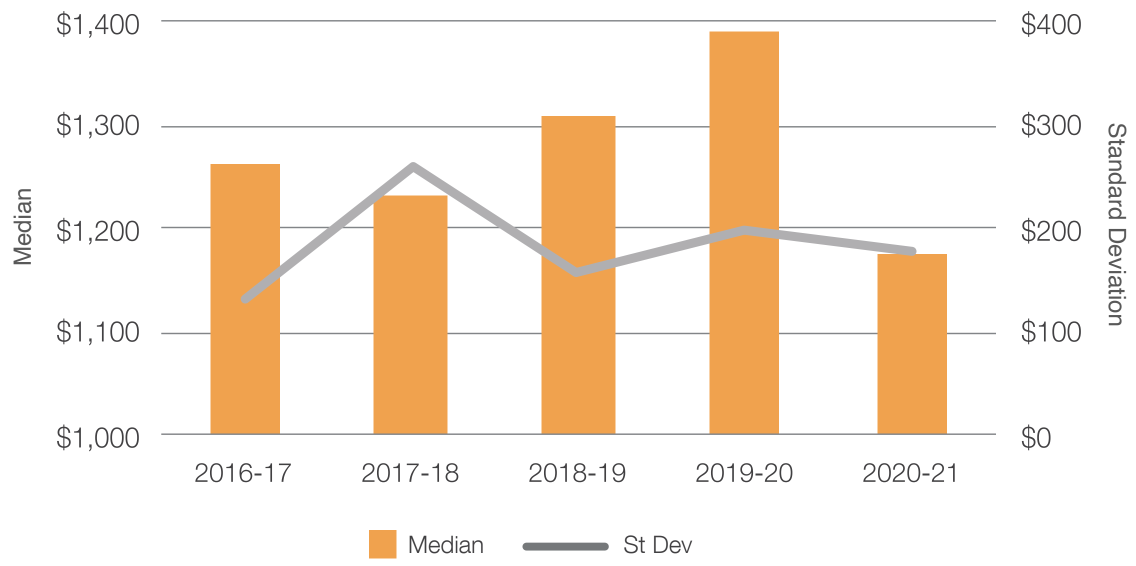


Figure 16 – Median and standard deviation of medium retailers' residential electricity market offers (2016-17 to 2020-21, Jemena)

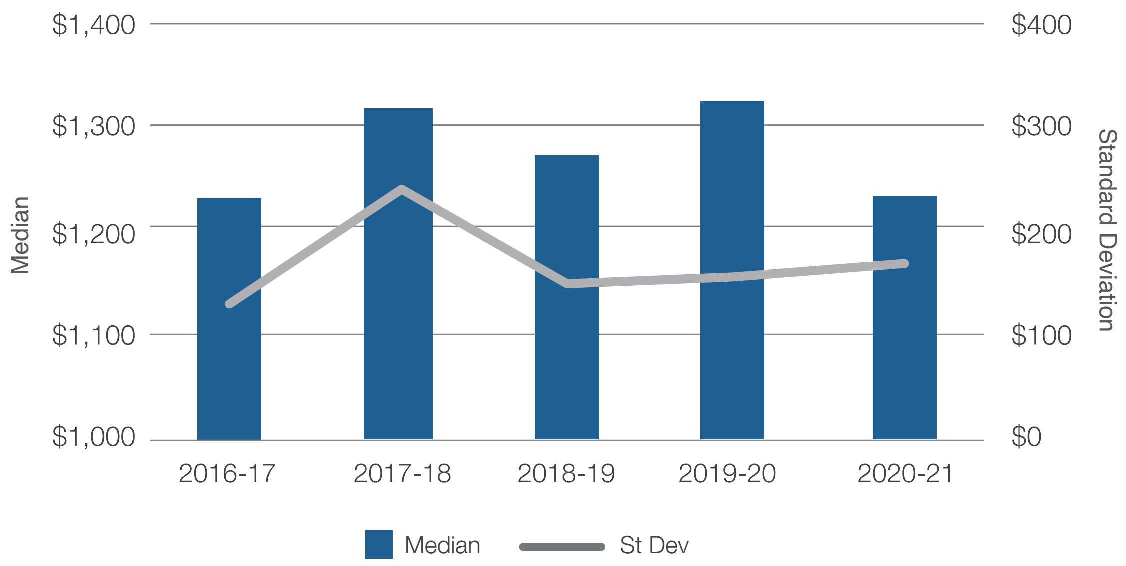
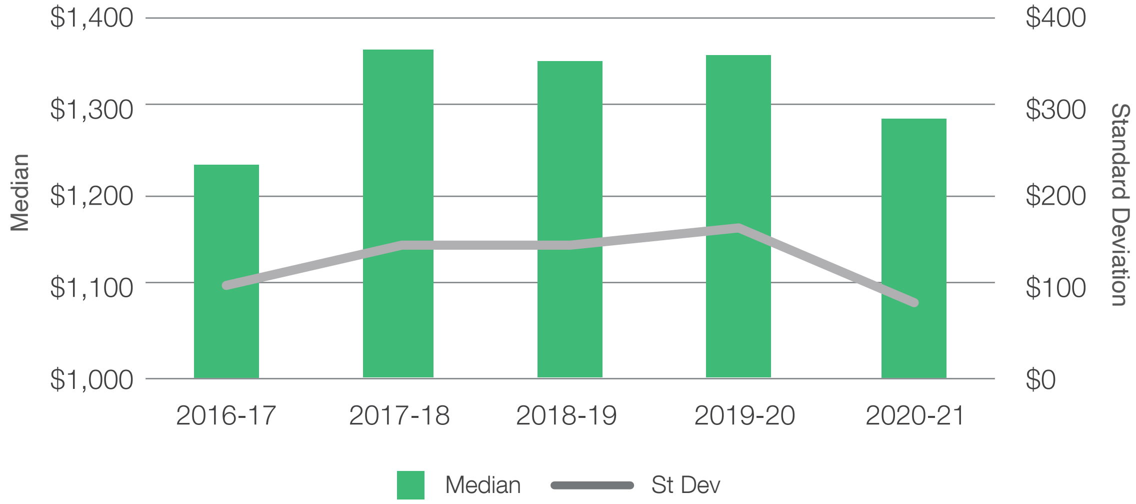


Figure 17 – Median and standard deviation of large retailers' residential electricity market offers (2016-17 to 2020-21, Jemena)



Switching off the (pricing) power

It may seem strange that large (prominent) energy retailers continue to hold a substantial share of the market while offering higher prices for a product that consumers cannot reasonably differentiate.

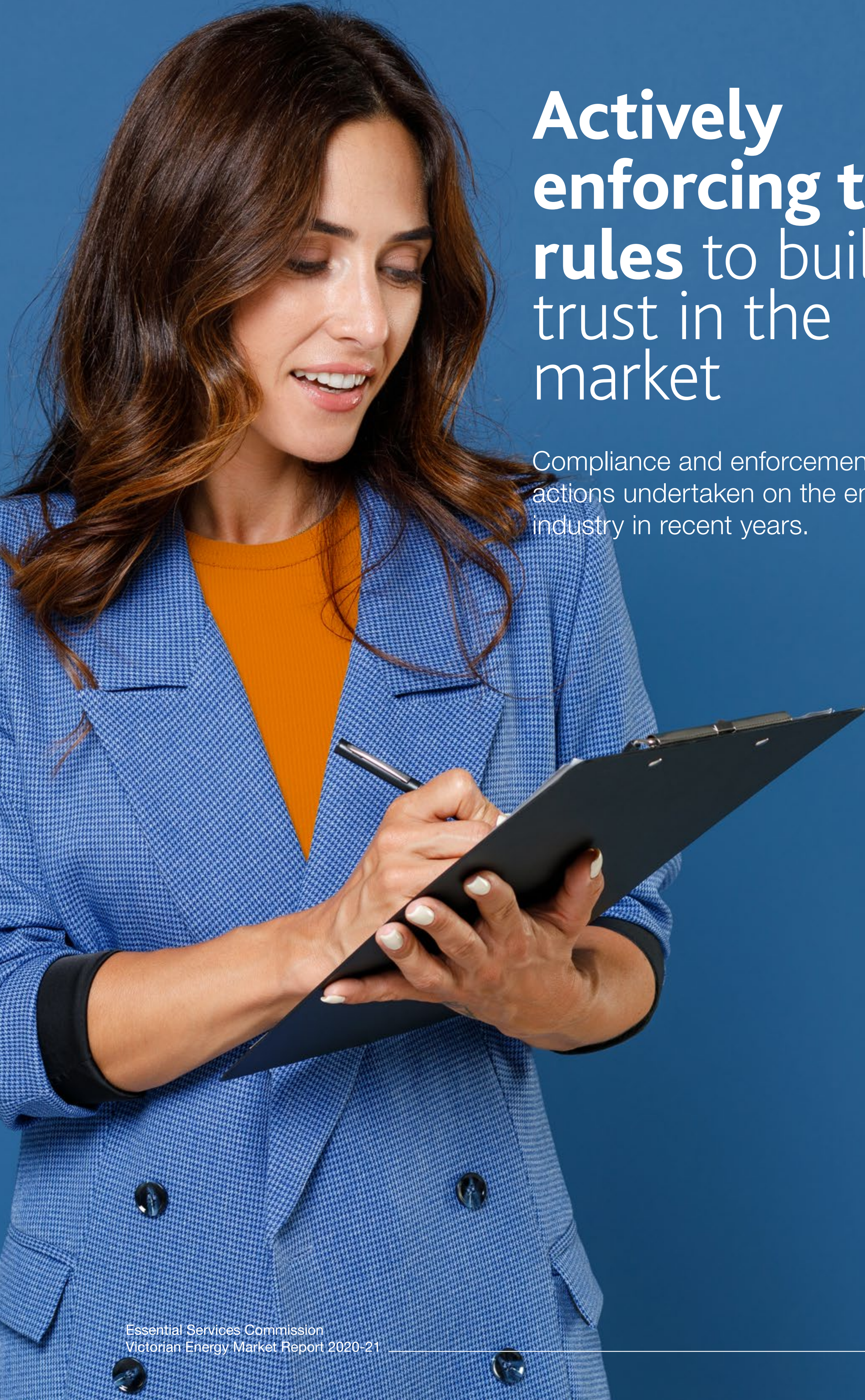
The reality is, as academic research and our own analysis indicates, these nuanced outcomes are partly driven by sophisticated consumers – with their own set of objectives and preferences – interacting with a complex market.

While consumer engagement alone cannot overcome the observed large retailer preference, genuinely considering the full set of available options when selecting an energy retailer could result in cheaper prices. More importantly, energy retailers have an important competition role in the energy market.

First, it is essential that all energy retailers compete on most customers' top concern: price. Second, small and medium retailers might attract and retain more customers by improving the non-price qualities of their offers. Without competition across both price and customer experience dimensions, customers may be less likely to trust the market.

In Victoria, there appears to be the right conditions for competition, but we are seeing there is a long-standing preference for large retailers for various reasons.

Going forward, actions that help increase customers' confidence and trust across all energy offer options will support access to the most competitive energy prices in the market.



Actively enforcing the rules to build trust in the market

Compliance and enforcement actions undertaken on the energy industry in recent years.

The introduction of new enforcement powers in 2016 came at a time of significant reforms to the Victorian energy rules, as well as the building of our capability as an enforcement regulator. It also saw the 2019 appointment of a new commissioner with a focus on enforcement, Sitesh Bhojani.

Over the past years, we have increased our enforcement action, with a particular focus on serious harms experienced by Victorian consumers due to alleged contraventions to the energy rules. Penalty payments have been steadily increasing – since 2018-19, energy businesses have paid more than $13 million in penalties (which includes almost $8 million paid in 2021-22 at the time of releasing this report). These penalty amounts highlight our concern for poor behaviour within the industry, such as fraudulent marketing, unfair pricing and charging, and contravention of rules designed to protect and assist customers experiencing vulnerability.

As the Victorian regulator of essential services, we will continue to monitor and act on non-compliance, and remain focused on both addressing key harms and acting in the long-term interests of consumers, particularly those who experience vulnerability. Another ongoing aim as a regulator is to see improved voluntary compliance and prevention of contraventions in the market.

We remain committed to providing further guidance and education for industry to act in compliance with their obligations and the interests of Victorian consumers. However, serious enforcement action is warranted where significant harm is caused to specific customers. This ensuring of accountability also builds consumers' trust and improves business confidence to invest in compliant operations, ensuring a level playing field in the market.

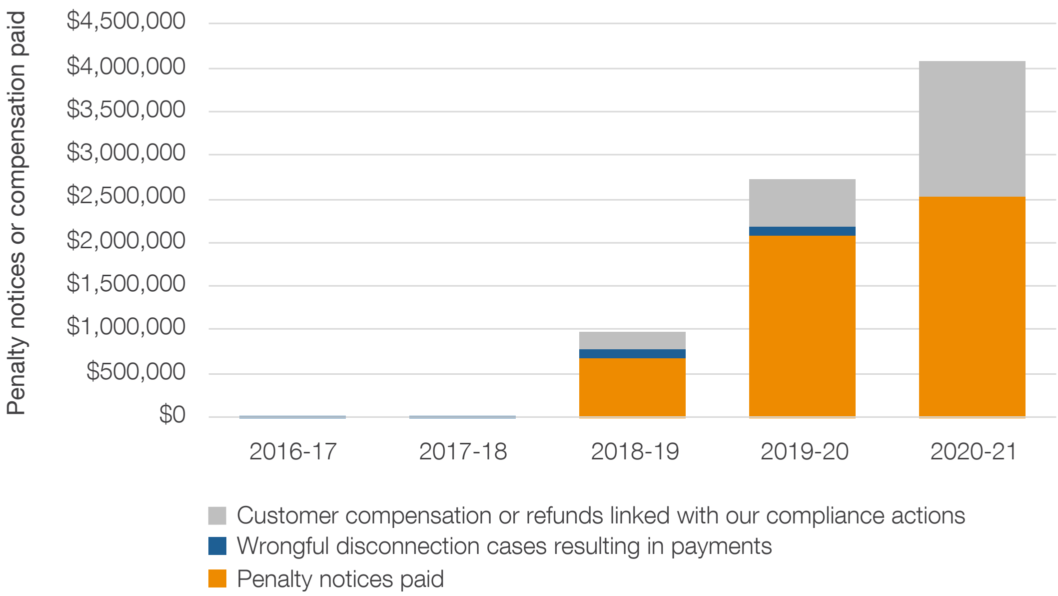
$13 million

in penalties paid by energy businesses since 2018-19

Increasing enforcement action to improve trust in the market

In 2020-21, over $2.5 million dollars were paid in penalties by energy companies. Our increased enforcement action in recent years demonstrates our commitment to protecting the long-term interests of Victorian energy consumers.

Figure 1 – Payments made to customers and penalty notices paid by energy businesses since 2016-17



Note: An additional $7,955,000 in penalties were also paid in 2021-22 at the time of releasing this report.

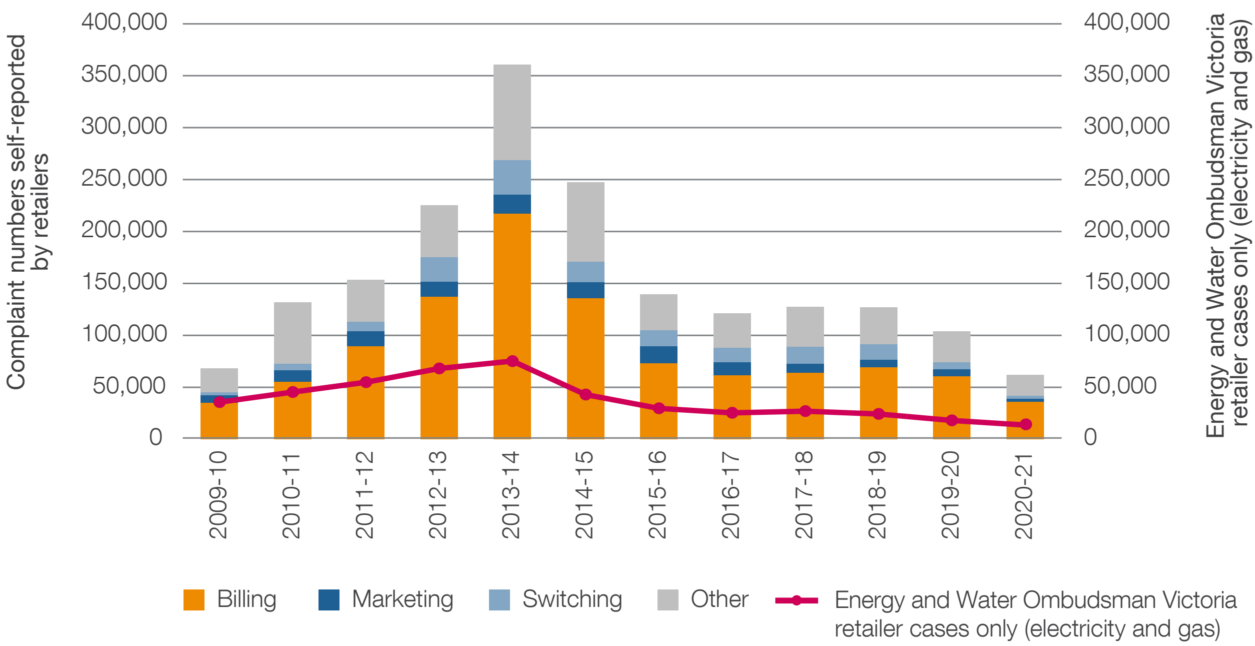
Poor behaviour on the part of retailers can damage consumer trust in the market and hamper confidence in the industry. This can create barriers between consumers and retailers in relation to resolving issues, searching for lower-priced energy offers, or exploring innovative products and services in the market. Surveys we conducted during 2020 found that 14 per cent of Victorians had negative experiences when contacting their energy providers for assistance, with one in five reporting that it was too hard or not worth it to seek a better deal.

Victorian consumers did report relatively modest perceived trust levels of energy retailers, rating around 7 on a scale of 10.[1] Energy Consumers Australia's long-term consumer sentiment surveys also indicated improved consumer satisfaction and confidence since 2019.

The number of Victorian electricity consumers being satisfied with value for money increased from 46 per cent to 73 per cent. The number of Victorian consumers being confident that the market is working in their interests rose from 30 per cent to 42 per cent, despite this metric of confidence remaining low.[2]

We also noted a decrease in consumer complaints and cases reported to us or presented to the ombudsman for dispute resolution. These indicators show possible improvement in the market, particularly after significant reforms of the Victorian retail energy rules.

Figure 2 – Complaint numbers reported by retailers and cases with the Energy and Water Ombudsman Victoria (retail electricity and gas)



14%

of Victorians had negative experiences when contacting their energy providers for assistance

7/10

of Victorian consumers did report relatively modest perceived trust levels of energy retailers

46–73%

increase of Victorian electricity customers being satisfied with value for money

1 Consumer Policy Research Centre (CPRC), Victorian Energy Insights Report – October 2020, CPRC, 2020, p 6.

2 Energy Consumers Australia (ECA), Sentiment Survey: June 2021, ECA, 2020.

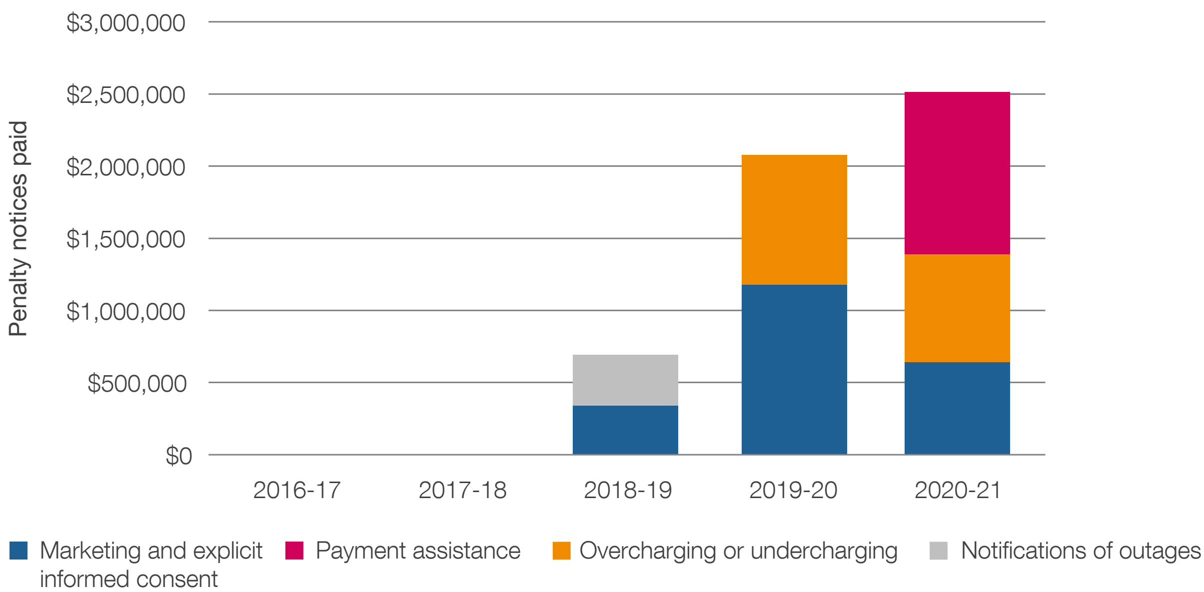
However, there is room for improvement. In comparison with the water sector (which we also regulate), 93 per cent of cases handled by the Energy and Water Ombudsman in 2019-20 were from the energy sector, while only 6 per cent were from the water sector. In surveys that specifically compare the energy sector with other industries, consumers' perceptions of energy businesses are average. In its survey of Australian consumers during 2020, the Consumer and Policy Research Centre found that the energy sector ranked third against other sectors,[3] with an average score of 5.1 out of 10 in overall experience rated by consumers.[4]

One of our key roles as the Victorian energy regulator is to ensure protections are being afforded to consumers under the rules, and to act when this appears not to be the case. Our focus is to address key areas of consumer harm, and deter future non-compliance by the sector.

In 2020-21, we focused our enforcement action on key consumer harms that also align with strategic priority areas. As shown in Figure 3, we issued substantive penalty notices addressing alleged poor marketing behaviour, overcharging of customers, and improper provision of assistance for customers experiencing payment difficulty.

This follows similar enforcement actions we took in 2019-20, but also shows our increased attention on protections for customers experiencing vulnerability. We also continue to actively monitor any potential distribution-related contraventions, particularly if these relate to customers using life support equipment.

Figure 3 – Penalty notices paid since 2016-17, by type of potential contravention



In 2019-20

93%

of cases handled by the Energy and Water Ombudsman were from the energy sector

The energy sector

ranked 3rd

against other sectors in the Consumer and Policy Research Centre survey during 2020

Average score of

5.1/10

in overall experience rated by Australian consumers during 2020

3 Other sectors' overall experience scores were as follows: mortgage at 6.3, insurance at 5.3, private rental at 4.8, telecommunication at 4.6, and credit/finance at 4.6

4 CPRC, *COVID-19 and Consumers: Sector Scorecard*, CPRC, 2021, p 5.

Marketing and signing up new customers

Click Energy paid **$640,000 in penalties** for allegedly failing to obtain explicit informed consent before signing up customers.

Billing and charges

Powershop paid **$300,000 in penalties** for allegedly price discriminating against solar customers.

AGL paid **$450,000 in penalties** for allegedly failing to explain undercharged amounts to customers before recovering those charges.

Almost **$1.5 million refunded** to **142,336 customers** for incorrect additional retail charges, **3 embedded network customers** overcharged and refunded.

Over **$52,000 refunded** to **2,316 customers** for failing to receive best offer messages on their bills.

Protections for customers experiencing vulnerability

Alinta paid **$1,250,000 in penalty** notices for allegedly making access to assistance difficult for customers.

9 wrongful disconnection dispute cases resolved, with **$21,525 being compensated** to customers

14 family violence policies reviewed, with improvements made to two retailers' policies

Energy company	Penalty notices	Penalty paid	Alleged contravention
Alinta	75	$1,125,000	Allegedly required customers to provide personal or financial information before providing payment assistance
AGL	30	$450,000	Allegedly failing to explain undercharged amounts to customers (particularly relating to concession entitlements) before recovering those charges.
Powershop	15	$300,000	Allegedly discriminating renewable energy customers (such as those with solar rooftop systems) by not offering the same tariffs offered to non-renewable energy customers
Click Energy	32	$640,000	Allegedly failing to obtain explicit informed consent before transferring a customer

Substantive penalties for poor marketing behaviour

One of the fundamental protections for energy customers in Victoria are rules ensuring customers are correctly informed and able to give explicit informed consent when switching energy contracts.

Since August 2018, we have issued penalty notices for failures to obtain explicit informed consent prior to contract formation with a customer. In 2020-21, Click Energy paid $640,000 in penalty notices for alleged fraudulent behaviour after an external sales agent supposedly faked customer details to sign up new customers.

In July 2021, Simply Energy recently paid $2.5 million in penalties for external sales agents' alleged fraudulent transfer of around 500 energy customers. We remain concerned about continuing fraudulent behaviour in the sector, particularly in relation to external sales agents which are, under the rules, the responsibility of retailers.

Our strong enforcement action in this area aims to encourage improved industry practices when marketing to customers, which will improve business confidence particularly for retailers that have invested in appropriate systems and training to support a compliance culture.

Addressing incorrect charging of customers and energy pricing

Energy consumers rely on retailers for the use and payment of energy as an essential service. It is particularly important that customers are being correctly charged and receive transparent pricing for energy – a key business activity of energy retailers.

If energy pricing is not transparent, or customers experience persistent and regular incorrect charging for their energy bills, this can erode consumer trust and confidence in the market.

In 2020-21, we were made aware of several problems relating to price fairness, price transparency, and billing accuracy. Powershop paid $300,000 in penalty notices for alleged price discrimination to customers with renewable energy (such as rooftop solar systems). In addition, Powershop had allegedly not offered renewable energy customers the same energy tariffs, terms and conditions that it offered to non-renewable energy customers.

We identified potentially incorrect fees being charged to standing offer and Victorian Default Offer customers.

Over 142,000 customers were refunded a total of $1,449,670 by five retailers – AGL (refunds of $1.4 million), EnergyAustralia, Powerdirect, Next Energy and BlueNRG. This covered fees for paper bills, debit/credit card fees and over the counter charges.

Besides the issuing of penalties, we also act on potential non-compliance and seek to remedy some of the harms caused to customers. This could lead to refunding customers who experience some financial loss due to potential contraventions of the rules. Five retailers – AGL, Powerdirect, Energy Locals, Tas Gas and Momentum – also refunded a total of around $52,000 to over 2,300 customers for allegedly failing to include best offer messages on customer bills.

We also took compliance action in response to consumer feedback, resulting in Sumo Power increasing the prominence of their 'best offer' message on its energy bills.

Increased focus on protections for consumers experiencing vulnerability

We have a particular commitment to consumers experiencing vulnerability and payment difficulty, and the *Essential Services Commission Act 2001* specifically requires us to consider vulnerable and low-income consumers in our decision-making.

This is emphasised through past reforms we have made in the energy sector, including the payment difficulty framework and enhanced provisions on retailers to assist customers experiencing family violence. More recently, we have developed a strategy that aims to break down the barriers that block access to essential services such as energy.[5]

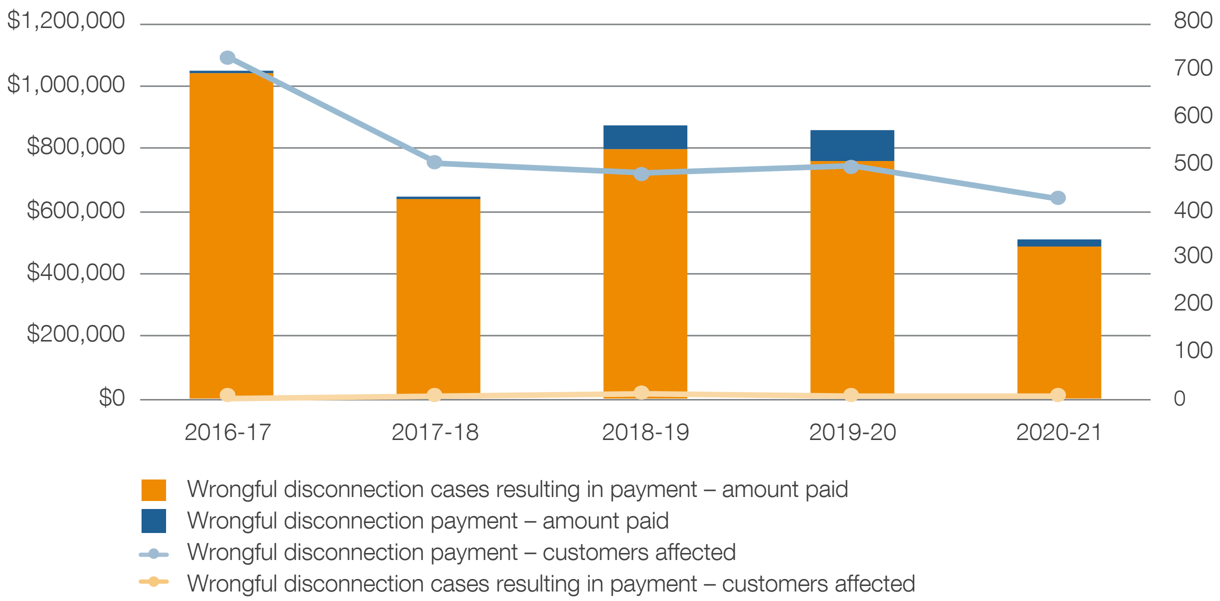
This focus has been evident in our compliance and enforcement actions during 2020-21. Alinta Energy paid $1.125 million in penalty notices for alleged contraventions of the rules relating to assisting customers in payment difficulty. Under our payment difficulty framework rules, customers are entitled to receive assistance without having to provide personal or financial information to the retailer or third parties (such as financial counsellors).

We have developed a strategy that aims to break down the barriers that block access to essential services such as energy.

If retailers add conditions to customers seeking help, this reduces the trust of consumers in energy retailers and creates barriers to accessing the support that customers are entitled to. We will act strongly to deter this behaviour so that the rules work in the way we intended.

We also issued penalty notices to AGL, which paid $450,000 in penalties for allegedly failing to explain undercharged amounts to customers before recovering those charges. This billing issue particularly affected more than six thousand Victorian pensioners and other concession holders. The alleged mistake led to these customers being issued unexpectedly high energy bills, with customers receiving letters and follow up bills with additional charges to recover the accidental undercharging, but not explaining the extra costs.

Figure 4 – Wrongful disconnection payments made by retailers since 2016-17



5 Essential Services Commission (ESC), *Getting to fair: Breaking down barriers to essential services*, ESC, 2021.

It is important that retailers clearly communicate to customers on energy charges, particularly for customers who are potentially experiencing payment difficulty or vulnerability.

There are also specific rules relating to the disconnection of customers from energy, which is an essential service for Victorians. If these rules are not followed and result in a customer's disconnection, retailers are obligated to report these events and compensation made to customers as a result.

We have noticed a reduction in recent years of wrongful disconnection payments made by retailers. During 2020-21, 425 customers were paid a total of $428,725 in compensation, the lowest number in five years (Figure 4). Some cases of wrongful disconnection are also referred to the commission, particularly if an outcome cannot be resolved between the retailer, customer and the Energy and Water Ombudsman of Victoria.

In 2020-21, we resolved nine cases relating to potential wrongful disconnection, resulting in $21,525 in compensation being paid to four customers. We also noted a reduction in the number of cases and compensation from resolved cases, down from $79,109 in 2018-19 and $101,440 in 2019-20. It is also important to note that in 2020, there was a significant reduction in disconnections for non-payment. This was in line with our expectations during Victorian government mandated movement restrictions during the coronavirus pandemic.

While this reducing trend of wrongful disconnection is welcome, the seriousness and harm of wrongfully disconnecting customers – particularly those who are experiencing vulnerability or payment difficulty – remains our focus. Over 400 customers are still affected by being wrongfully disconnected each year, despite the specific rules we designed to ensure that disconnections are only a last resort.

We also remain committed to protecting energy customers experiencing family violence, which follows particular rules for energy retailers we introduced in 2019. In 2020-21, we reviewed the family violence policies of 14 retailers, which resulted in two retailers' policies being improved.

Supporting improved compliance and practices of the energy industry

Our ongoing aim is to improve the practices across the energy industry by promoting voluntary compliance, and we will continue to take compliance and enforcement actions to address harm.

We strive to see an energy market with integrity – one that has the trust of Victorian consumers to engage in the market, and to give energy businesses confidence and certainty to follow the rules and invest in a positive compliance culture.

In 2020-21 we developed nine guidance notes for the industry. These were designed to clarify existing rules to help improve compliance so that energy businesses may meet our intentions and expectations of these rules. These guidance notes directly relate to the key areas of customer harm addressed during the year. One relates to price discrimination of solar customers, one relates to appropriate retail charges for standard retail contracts, and seven clarify the rules that support customers in payment difficulty so that disconnection is a last resort.

Easing the burden of unpaid bills

Victoria's payment difficulty framework for energy consumers provides the strongest hardship provisions in the country.

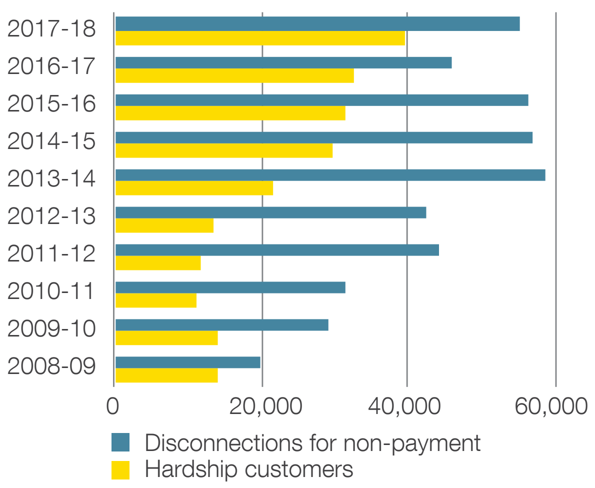
What have been the overall outcomes of the framework leading up to 2020-21?

Victoria's payment difficulty framework originated from a 2016 commission inquiry into the financial hardship programs of energy retailers. This came at a time of increasing numbers of both customers seeking assistance and customers being disconnected for not paying their outstanding bills (see Figure 1). The inquiry found that while there did not appear to be any widespread non-compliance with hardship programs, the support for consumers was inconsistent.

In 2019, after extensive consultation with the community sector and the energy industry, we introduced Victoria's payment difficulty framework – a series of rules that provide strong and more consistent hardship assistance for Victorian energy consumers.

The new rules ensured minimum entitlements to all customers (known as 'standard assistance') and further minimum entitlements to customers with arrears ('tailored assistance').

Figure 1 – Hardship customers and disconnections for non-payment (electricity and gas)



In 2019 we introduced Victoria's payment difficulty framework – a series of rules that provide hardship assistance for Victorian energy consumers.

What is the payment difficulty framework?

The framework aims to support energy customers paying off their energy arrears, and for disconnections of customers to occur only as a measure of last resort. It was designed to provide clear minimum entitlements of assistance for all customers, regardless of energy retailer.

The new rules removed many of the previous barriers to customers receiving assistance. Prior to the framework, customers had to provide personal and sensitive information about their circumstances before receiving assistance. Retailers also had more discretion to decide the timing and type of assistance offered to customers, and when it could be changed or withdrawn.

What standard assistance is available to all Victorian customers?

All Victorian customers can access help from their retailer to stay on top of their energy bills, such as:

- paying bills in different frequencies or amounts to manage the total bill
- delaying the payment of a bill (once a year)
- paying in advance.

What tailored assistance is available for customers experiencing payment difficulty?

For customers who can and cannot afford their energy usage, customers can access support including:

- a payment plan to pay off their energy debt (over a period of up to two years)
- advice on how to repay arrears in two years
- advice and information about other support such as government assistance (including grants and energy concessions)
- information on future energy use and how this cost could be lowered.

For customers who cannot afford their ongoing use, further support can be accessed including:

- a pause on debt payments for up to six months and part-payments of future bills
- practical advice on reducing energy cost, such as checking current energy offers and providing advice on the best energy offer available
- practical help to reduce energy bills, such as energy audit or energy efficiency products.

More Victorian customers received assistance under the framework and in 2020-21

In the first year of the framework, consumers receiving assistance increased by around 36 per cent for electricity and 15 per cent for gas (between March 2018 and September 2019, as per Figure 2). In 2021, around 60,000 customers on average were receiving assistance each month.[1] This is a significant increase compared to around 39,000 to 44,000 customers in hardship programs in 2017-18.

These increases could be due to the framework, which now requires customers to receive information about assistance once they miss paying an energy bill. It is likely that customers not previously in hardship programs are now receiving assistance.

However, it is important to recognise that there are two distinct cohorts of customers who receive tailored assistance; those who can pay their ongoing use and those who cannot (see Figure 3).

In 2021, an increasing number of customers who can pay for their ongoing use received assistance, with a peak in the March 2021 quarter. Notwithstanding fluctuations during the coronavirus pandemic, the number of customers who receive assistance but cannot pay their ongoing usage remain stable and at similar levels since the beginning of the framework in 2019.

Figure 2 – Number of residential customers receiving assistance between 2017 and 2021

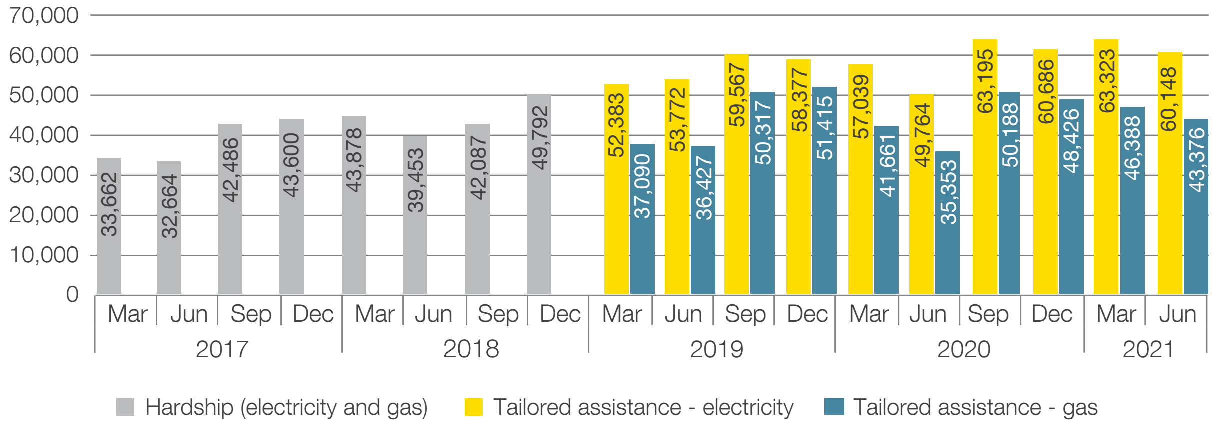
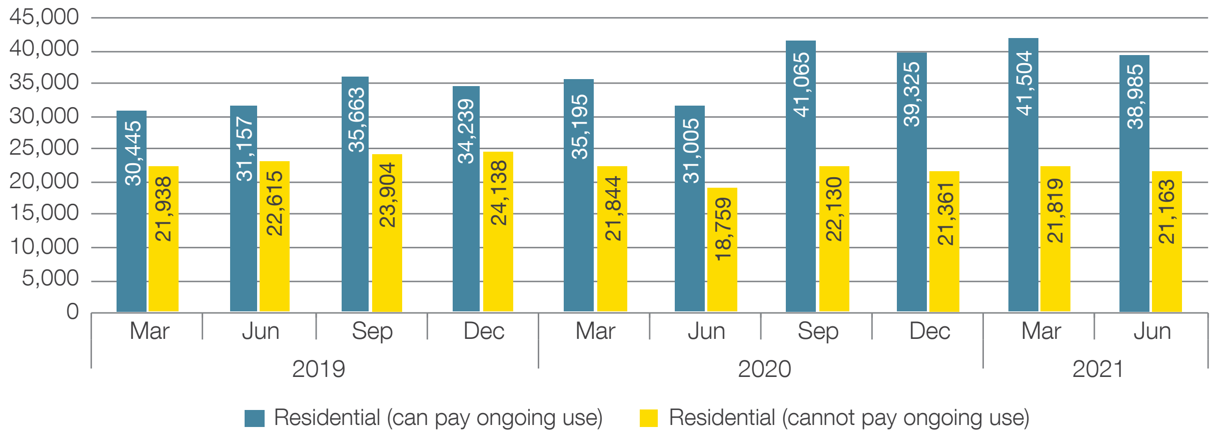


Figure 3 – Tailored assistance electricity customers



[1] We note that between March and September 2020, because of the coronavirus pandemic, some retailers offered customers the ability to defer the payment of energy bills, which appears to have resulted in a reduction in tailored assistance customers. Numbers of tailored assistance customers then increased to stable levels in 2021.

Varied trends of customer arrears when receiving assistance

In 2016, the hardship inquiry found that previous hardship programs were generally ineffective at preventing customers from accumulating further arrears.[2] The framework has been designed so that customers can receive timely assistance, with the ability to propose and revise payment arrangements over time.

Our early analysis indicates that on average over the past few years, the arrears of customers receiving assistance have remained relatively stable, particularly for customers who can pay their ongoing use (Figure 4).

We also note that the arrears of customers who cannot pay their ongoing usage have increased in 2021 (Figure 5), with the increase in March 2021 coinciding with the removal of federal government income support payments. It is important to remember that these customers are likely to be on payment arrangements where the payment amount is less than their ongoing consumption. In some cases, these arrears can also be put on hold to help a customer catch up with their new bills. While this assistance helps a customer stay in contact with their retailer, it can contribute to increased arrears over time.

Figure 4 – Average arrears of customers receiving tailored assistance who can pay ongoing use

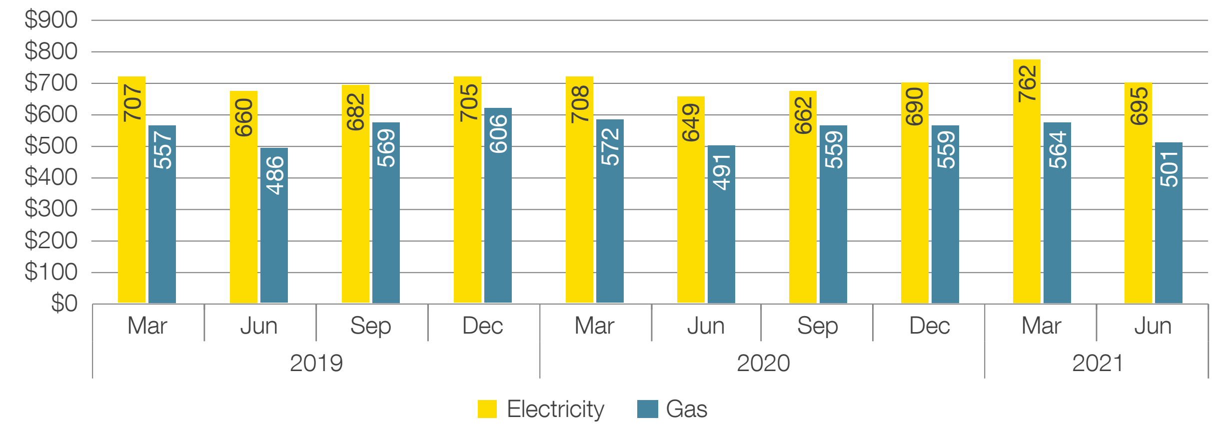
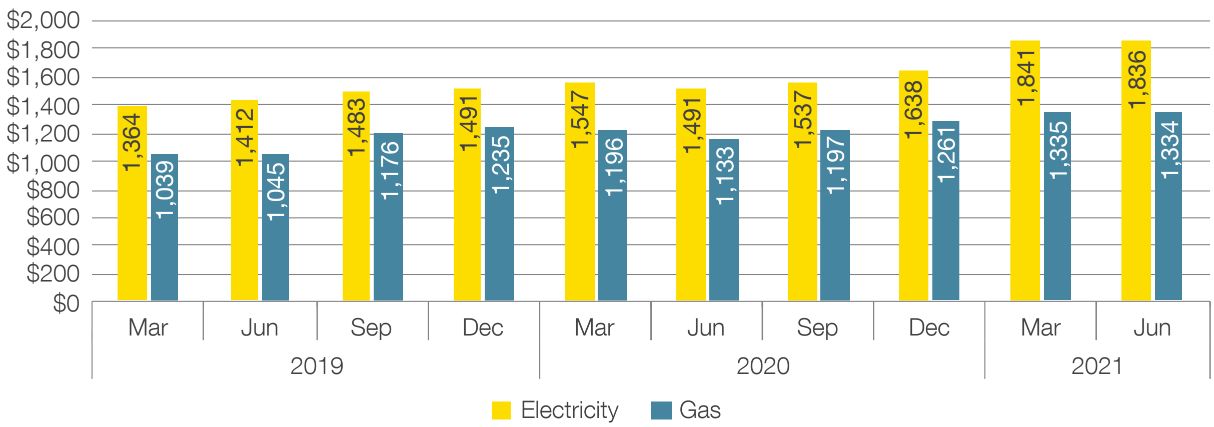


Figure 5 – Average arrears of customers receiving tailored assistance who cannot pay ongoing use



[2] Essential Services Commission (ESC), *Supporting customers, avoiding labels: Energy hardship inquiry final report*, ESC, 2016, p 10.

Customers access assistance only after accruing relatively high levels of arrears

The importance of early engagement with households who are struggling to pay their energy bills was highlighted in our 2016 hardship inquiry. It also revealed that customers on hardship programs consume more energy than other customers, demonstrating how quickly debts can accrue over a shorter period for these customers.

Between 2013 and 2018, there was an increasing proportion of customers entering hardship programs with higher levels of energy debt (see Figure 6).

The payment difficulty framework encourages retailers to be more proactive and responsive to a customer's arrears. To prevent accumulating arrears before receiving assistance, retailers must now provide customers with information about the assistance available to them once they miss paying an energy bill.

It was found that customers were starting assistance at varying times, and in some instances with already high debt.

Since 2019, customers have begun receiving assistance at around $920 for those who can pay for their ongoing use – this has not changed over the last two years. However, for customers who cannot pay their ongoing use, there has been an increase in average arrears when commencing their assistance, recorded at $1,343 in 2020-21 (see Figure 7).

Figure 6 – Energy debt on commencing hardship program across the year, percentage of customers by debt-bracket

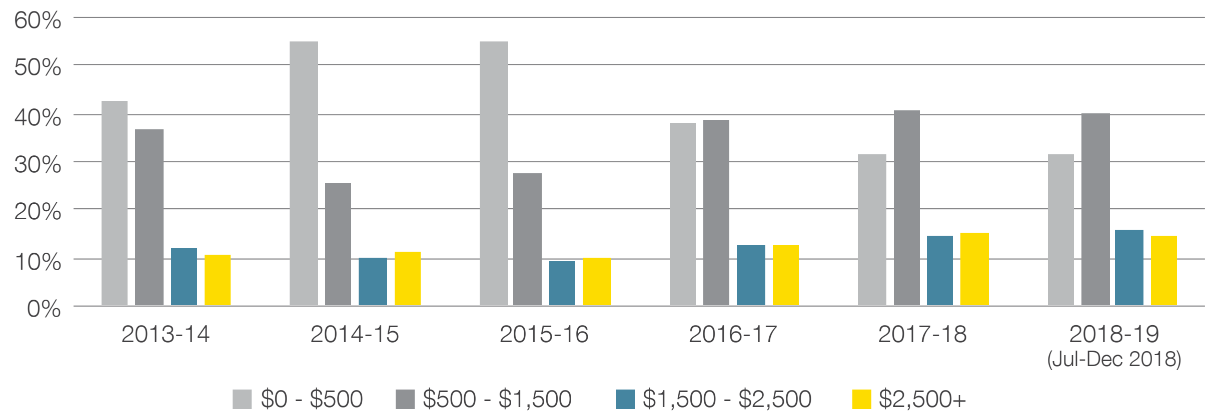
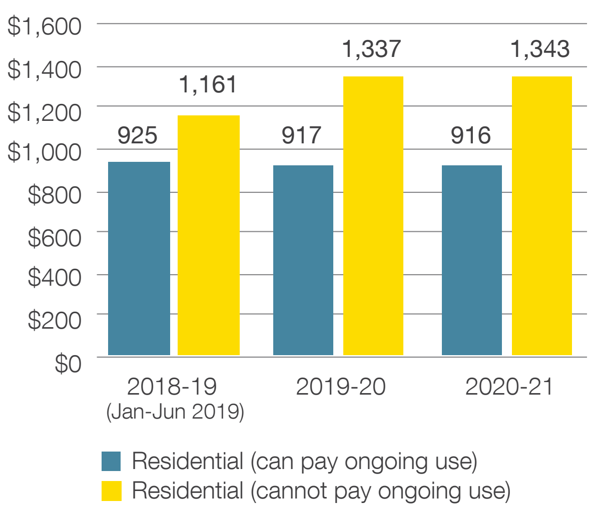


Figure 7 – Average electricity debt on commencing tailored assistance



On average, around 60 per cent of customers commence their assistance with more than $55 but less than $1,000 of arrears on average (Figure 8). It also appears that some customers (between 15 to 17 per cent) are receiving assistance with minimal levels of debt. However, there is notable variability between retailers – some have high proportions of customers starting their assistance with substantial levels of debt. We plan to undertake further analysis to better understand the drivers of these apparent differences (Figure 9 and Figure 10).

60%

of customers commence their assistance with more than $55 but less than $1,000 of arrears on average

Figure 8 – Debt on commencing tailored assistance in 2020–21, percentage of customers by debt-bracket

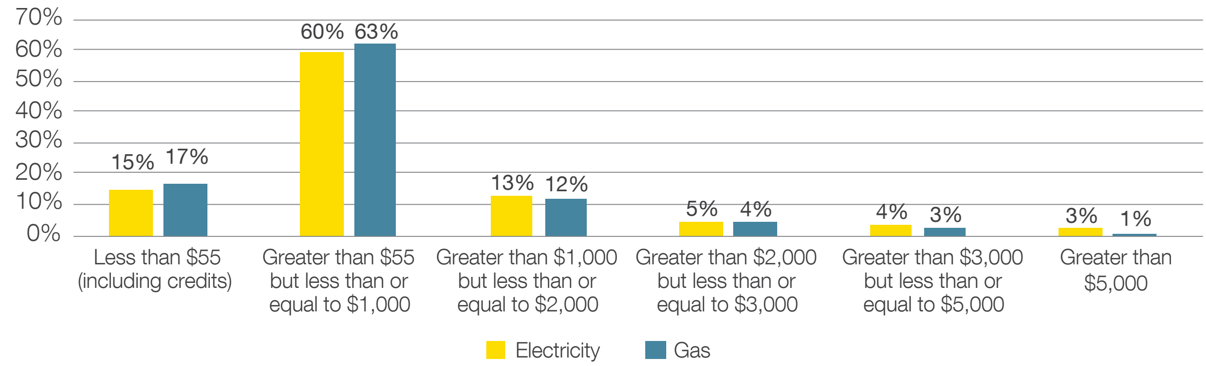


Figure 9 – Average electricity debt on commencing tailored assistance (can pay ongoing use), by size of retailer

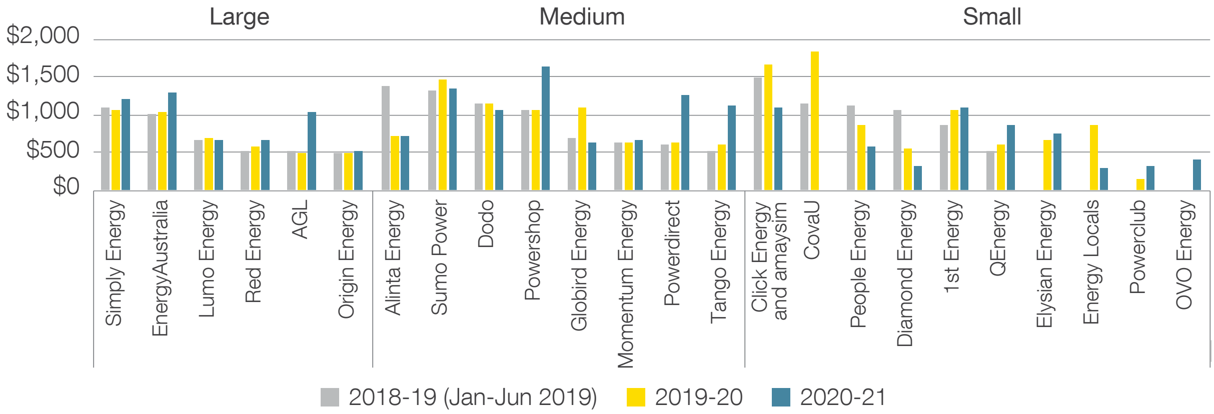
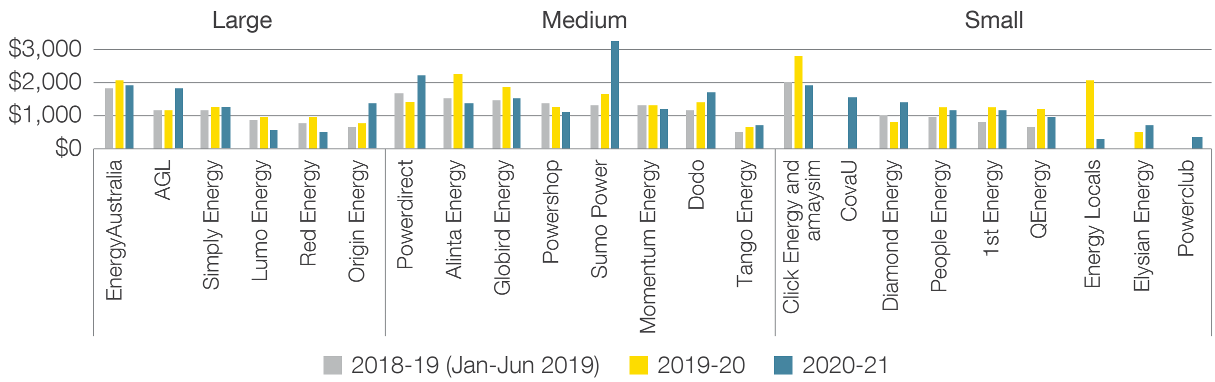


Figure 10 – Average electricity debt on commencing tailored assistance (cannot pay ongoing use), by size of retailer



Two-thirds of customers receiving assistance are also receiving energy concessions

Almost 1 million Victorian households received annual electricity concessions in 2020–21. This is an increase of around 12 per cent from the previous year, and equivalent to more than one in three of all residential electricity consumers.[3]

Victorian households can also apply to the Victorian government for temporary financial assistance with a utility relief grant.[4] The number of households receiving these grants has increased significantly, with nearly 69,000 residential electricity customers obtaining them over the last two years (see Figure 11).[5]

These grants are paid directly to the energy retailer to help reduce outstanding arrears for customers. Despite the large increases in customers receiving utility relief grants, we have not seen similar increases in tailored assistance customers accessing energy concessions. One in three customers who are receiving assistance and cannot afford their ongoing use did not access concessions in 2020–21. This has been relatively steady over the past two years (see Figure 12).

As part of our review of the framework, we are interested in understanding any differences between customers who access payment assistance, and those who receive government concessions or grants.[6]

Figure 11 – Number of utility relief grants and tailored assistance (who cannot afford ongoing use)

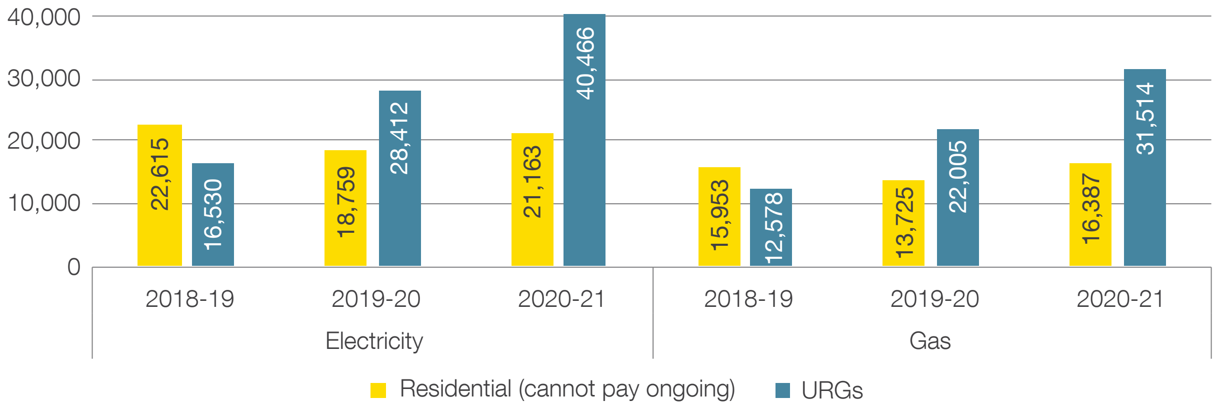
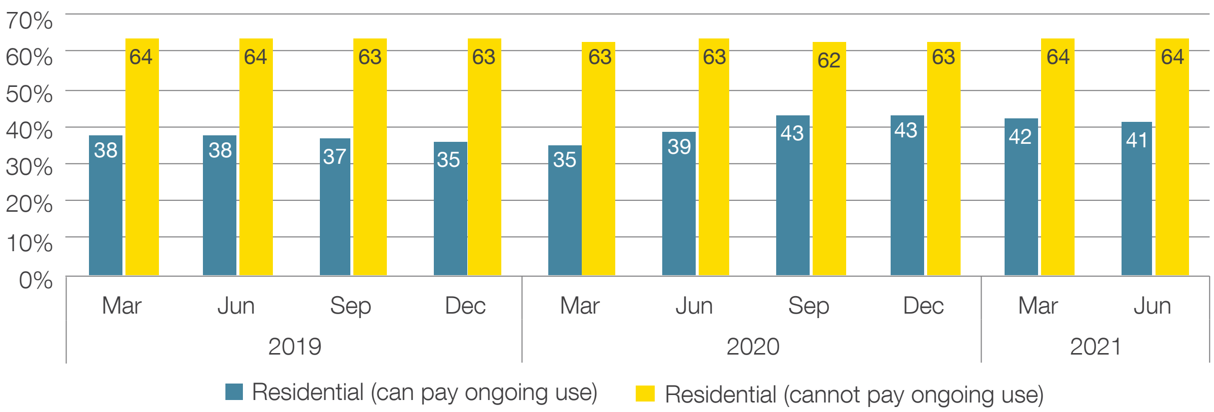


Figure 12 – Percentage of electricity customers on tailored assistance receiving an electricity concession



3 Victorian government energy concessions provide eligible Victorians with 17.5 per cent off their electricity or gas bills in relevant periods.

4 Utility relief grants provide up to $650 for electricity and gas separately (or $1,300 if a household has only a single source of energy) every two years. These grants are provided by the Victorian government.

5 In 2020-21, the Victorian government approved 21,469 URGs water applications.

6 Under the framework, retailers are obligated to check customers' concession status when first receiving tailored assistance, but there is no requirement to regularly check this going forward.

A third of customers successfully complete their assistance without debt

The framework allows room for retailers and customers to agree on payment terms for managing arrears. Customers can stop receiving this assistance for various reasons, such as having successfully paid off their arrears, or not being able to comply with payment terms.

In 2020-21, more than 172,000 electricity customers stopped receiving tailored assistance. This is a large turnover, given that around 60,000 electricity customers are receiving assistance at any given time in that year. Of these customers, around 30 per cent successfully paid off their arrears and no longer required assistance. However, 49 per cent of customers were unable to comply with their payment terms or no longer received assistance which placed them at risk of disconnection (see Figure 13).

> 172,000

electricity customers stopped receiving tailored assistance in 2020-21

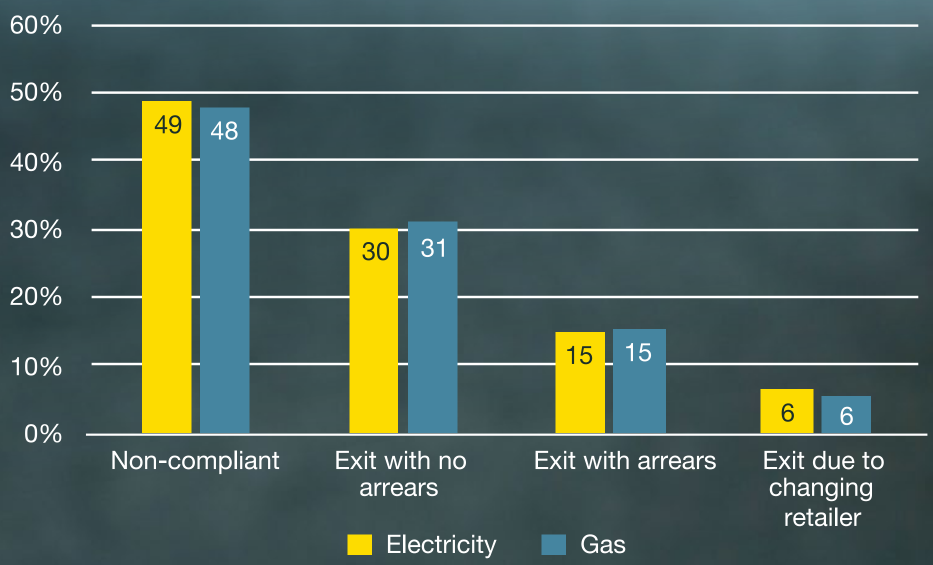
49%

of electricity customers were unable to comply with their payment terms or no longer received assistance

60,000

electricity customers are receiving assistance at any given time in that year

Figure 13 – Proportion of energy customers' reason for exiting assistance in 2020–21, by fuel

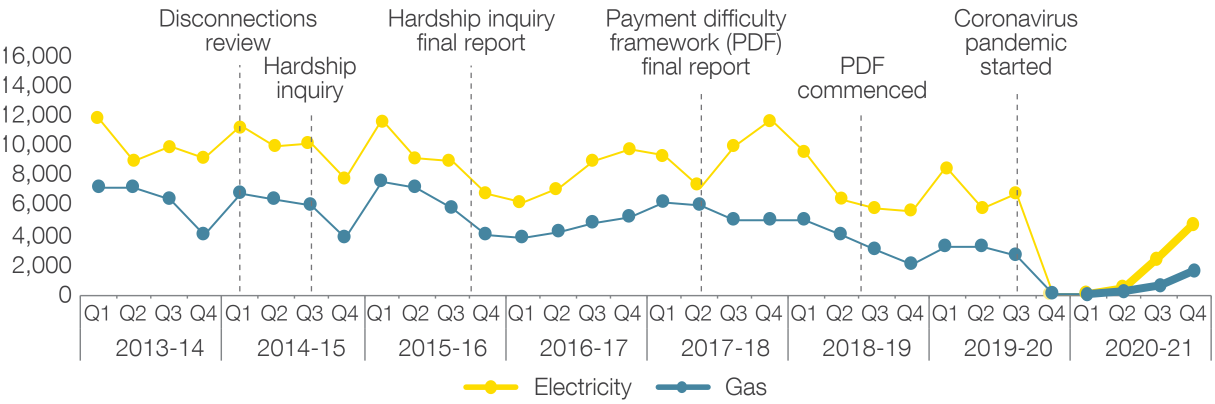


Disconnections for non-payment have decreased

Customers receiving tailored assistance are protected from disconnection. Once the framework began in 2019, we observed a noticeable decrease in the number of disconnections for not paying outstanding bills compared to 2018 (see Figure 14).

We also noted that there were hardly any disconnections in 2020. However, this was a result of our expectations for no disconnections to occur during Victorian government mandated stay-at-home restrictions (particularly between March and October 2020). The noticeable reduction in disconnections – particularly during 2019 – is a welcome sign, particularly as the framework has been designed to ensure that disconnection is only a last resort measure.

Figure 14 – Trend of disconnections for non-payment over the years



It is important to reiterate that a customer cannot be disconnected if they are receiving tailored assistance. In 2019-20, more than half of the customers disconnected were not receiving assistance in the six months leading up to disconnection (see Figure 15). This proportion increased in 2020-21 to 76 per cent of electricity customers who were disconnected.

We also observed that around 65 per cent of electricity customers who were disconnected for non-payment had a debt of more than $1,000 in 2021 (see Figure 16).

If a customer is disconnected for non-payment and subsequently engages with their retailer, a retailer can initiate reconnection of the customer's energy supply. More than half of disconnections for non-payment are reconnected within seven days of disconnection for electricity customers (see Figure 17). We note that because of smart meters, most electricity reconnections can be done remotely in Victoria, but gas reconnections require a site visit. Some customers may also find a new retailer in order to be reconnected, a scenario not covered in our analysis.

Figure 15 – Proportion of residential customers disconnected for non-payment, not receiving tailored or standard assistance in previous six months

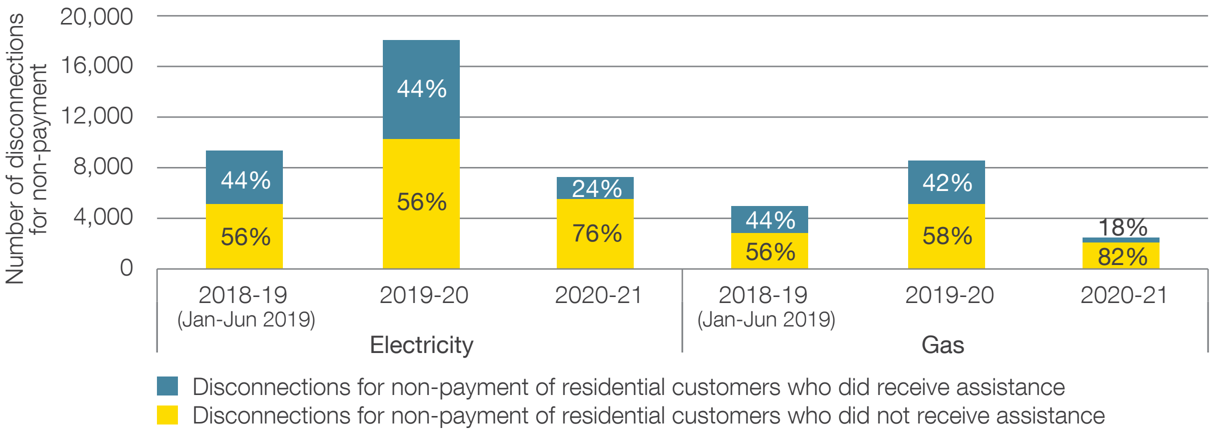


Figure 16 – Total arrears of residential customers (accounts) who were disconnected for non-payment in 2020–21

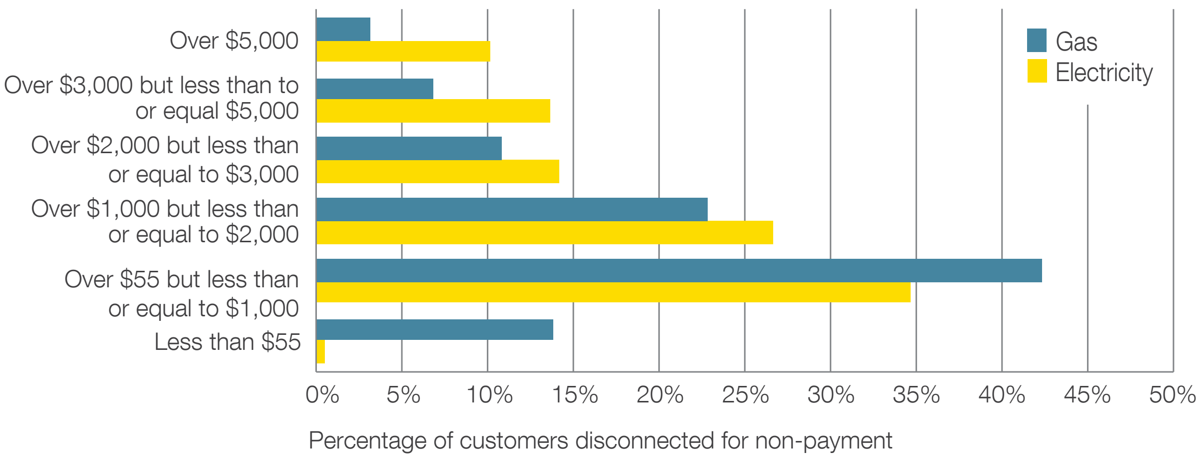
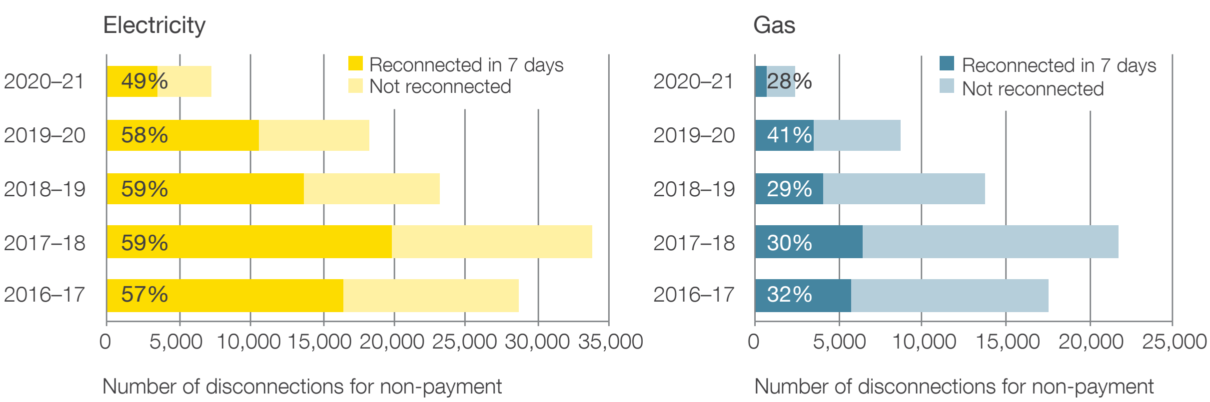


Figure 17 – Proportion of residential electricity and gas disconnections for non-payment which were reconnected by the same retailer within seven days



Reminder and disconnection warning notices, and reconnections

As part of making disconnections a last resort measure, the framework requires retailers to send various notices and information about assistance to customers before they can be disconnected. This includes a reminder notice and a disconnection warning notice, which can prompt the customer to engage with the retailer or pay their bill.

In 2019, around 120,000 electricity reminder notices and 50,000 electricity disconnection warning notices were sent every quarter. During the same period, around 5,400 residential electricity customers were disconnected each quarter. The number of notices sent to customers appears to remain stable up to 2021, apart from a noticeable drop in the September 2020 quarter during a long period of restricted movements in Victoria (see Figure 18). Large retailers, with the exception of Red and Lumo Energy, sent out the most electricity reminder and disconnection warning notices in 2020–21 (see Figure 19 and Figure 20).

Figure 18 – Residential electricity reminder and disconnection warning notices, by quarter

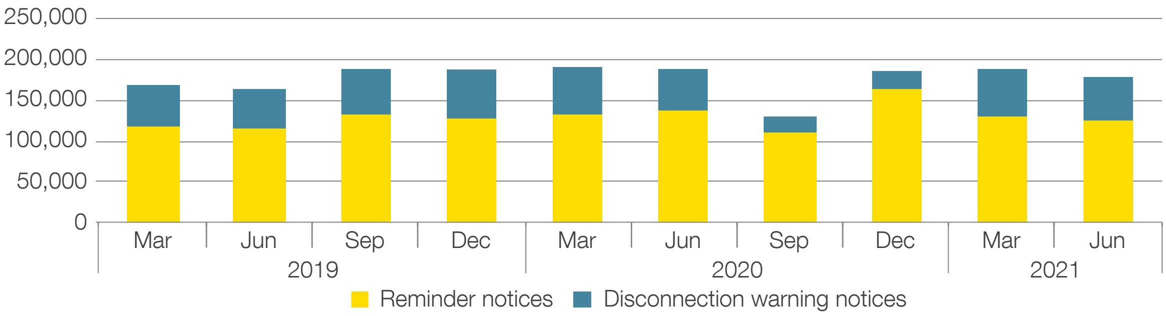


Figure 19 – Number of residential electricity reminder notices per 100 electricity customers in 2020–21, by retailer

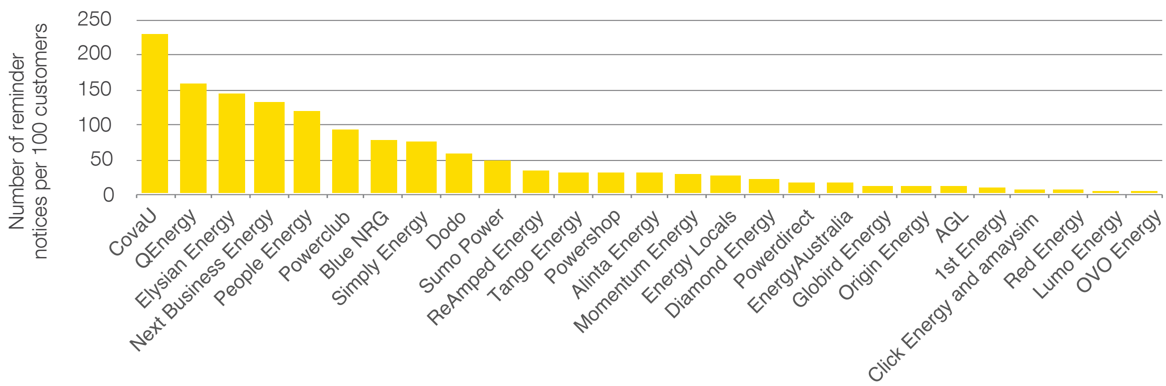
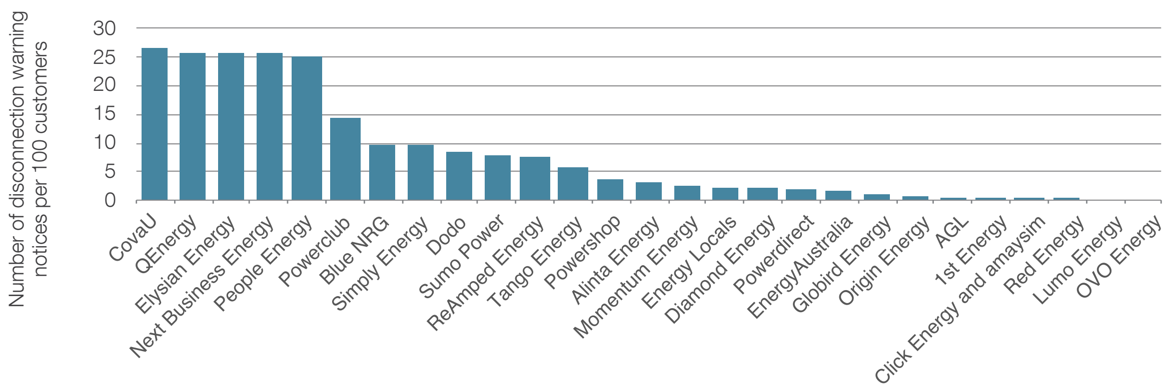


Figure 20 – Number of residential electricity disconnection warning notices per 100 electricity customers in 2020–21, by retailer



Collaborating to identify areas of improvement

We have seen some welcome results after two years of the framework's implementation. Although we appreciate that this has been a far from normal period, with both greater strains on many customers' finance, but also additional federal and Victorian government support.

Overall, more customers are accessing assistance when compared to past hardship programs, particularly customers who can pay their ongoing usage.

We have also seen a noticeable drop in disconnection levels since the beginning of 2019. We do recognise that there were very few disconnections in 2020, particularly in line with our expectations during government-mandated movement restrictions due to the coronavirus pandemic.

While these early indicators are welcome, we have also observed some signs that warrant further attention.

The average customer begins receiving assistance with high levels of arrears, and more than half of the customers being disconnected had not received assistance beforehand. These outcomes do vary across retailers, but we are keen to further understand examples of effective practices that mutually assist customers and help retailers manage debt.

These recent observations are timely, particularly as we review the implementation of the framework. As we continue to gather evidence and consider consumer feedback, we will be reporting our review findings in March 2022. We remain committed to work with the industry and the community sector, as well as to explore better practices that can help support the long-term interests of Victorians, particularly for those experiencing payment difficulty.

Victorian energy market snapshot

A visual summary of the performance of energy retailers and distributors

Energy offers and prices

Small Business Gas (Melbourne)

$9,308

representative annual bill based on median Victorian market offers

(Australian Gas Network central area)

Residential Electricity

$1,132

representative annual bill based on median Victorian market offers

(CitiPower distribution zone)

Residential Gas (Melbourne)

$1,349

representative annual bill based on median Victorian market offers

(Australian Gas Network central area)

Small business Electricity

$2,999

representative annual bill based on average of Victorian market offers

(CitiPower distribution zone)

-11.4%

change in the median estimated annual bill for residential electricity market offers in 2020-21

(CitiPower distribution zone)

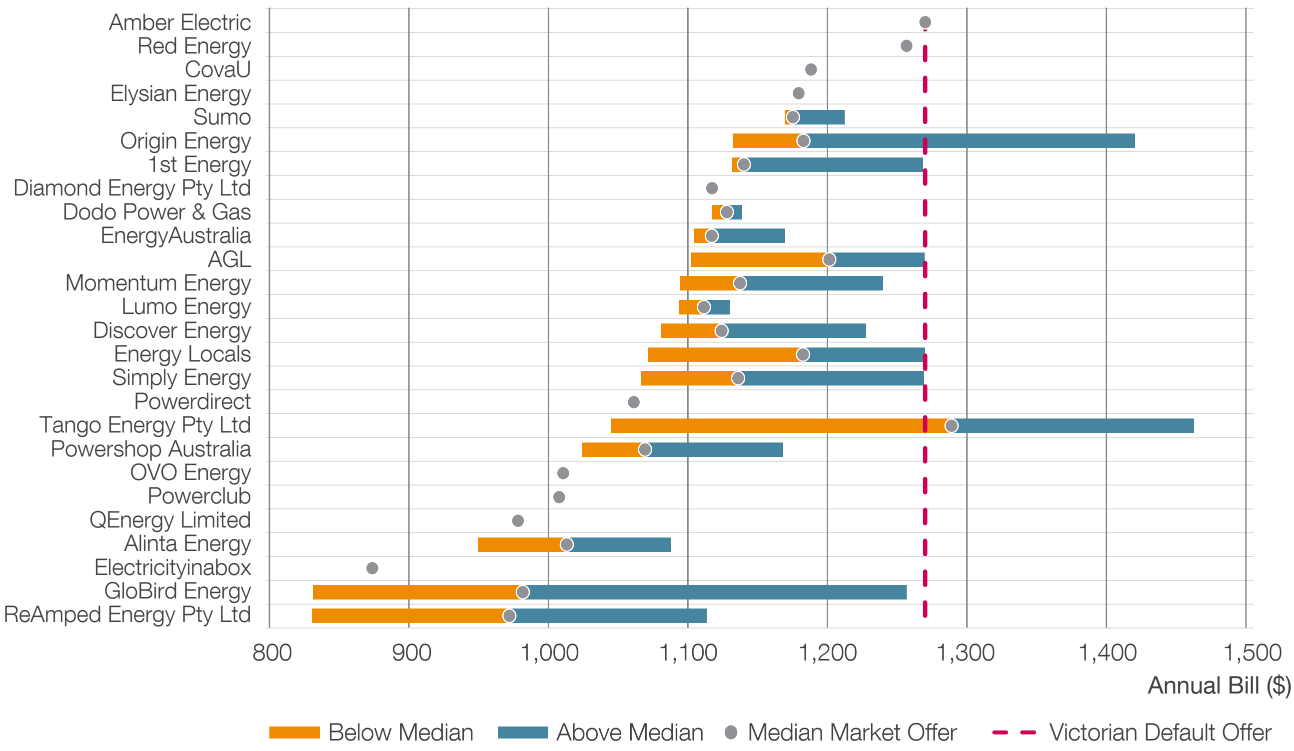
-2.7%

change in the median estimated annual bill for residential gas market. offers in 2020-21

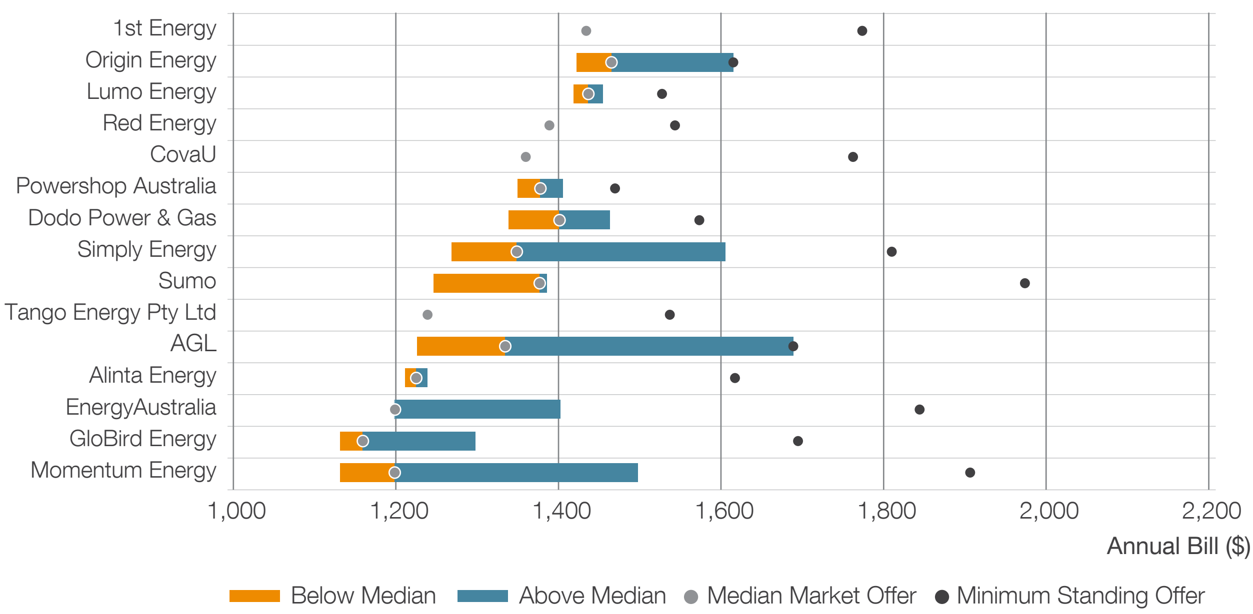
(Australian Gas Network central area)

Comparison of residential market offers in 2020-21

Spread of all market offers for residential electricity by retailer, for CitiPower (4,000 kWh)

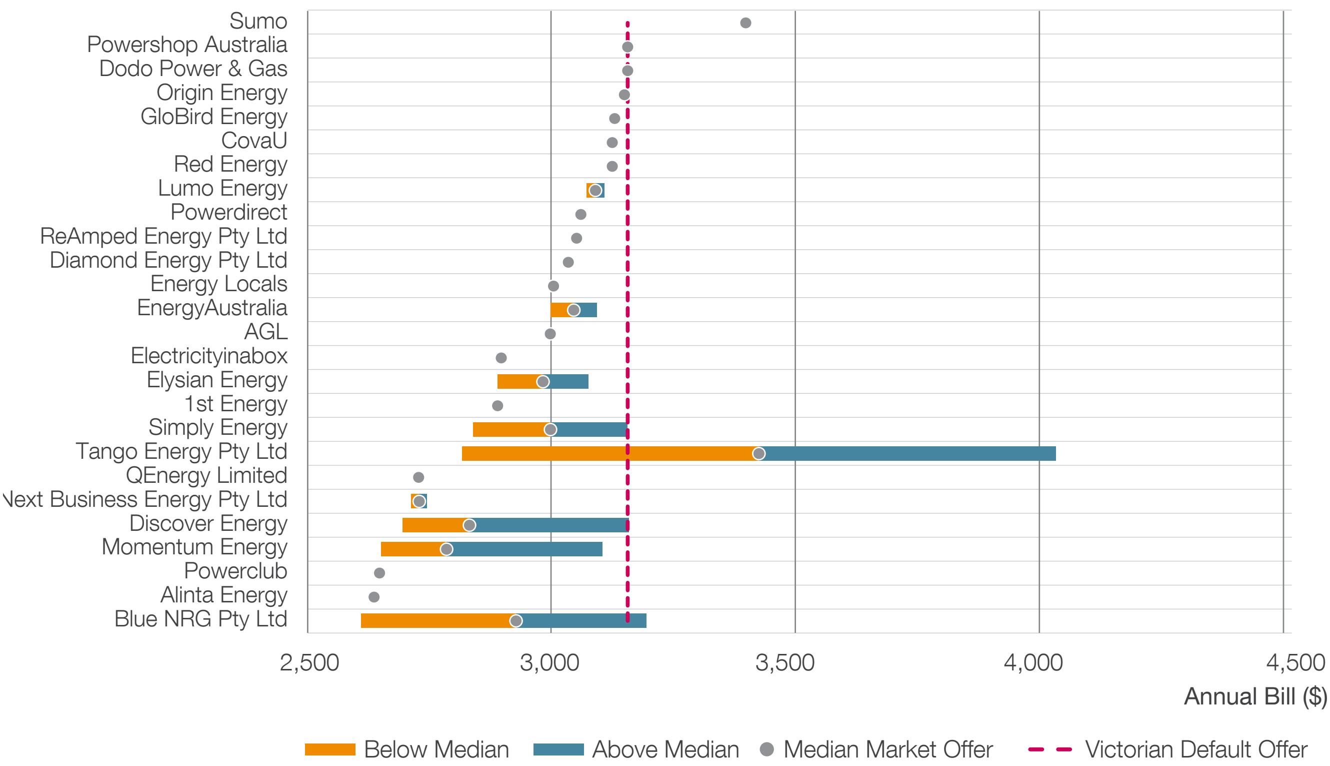


Spread of all market offers for residential gas by retailer, for Australia Gas Networks central area (54.4GJ)

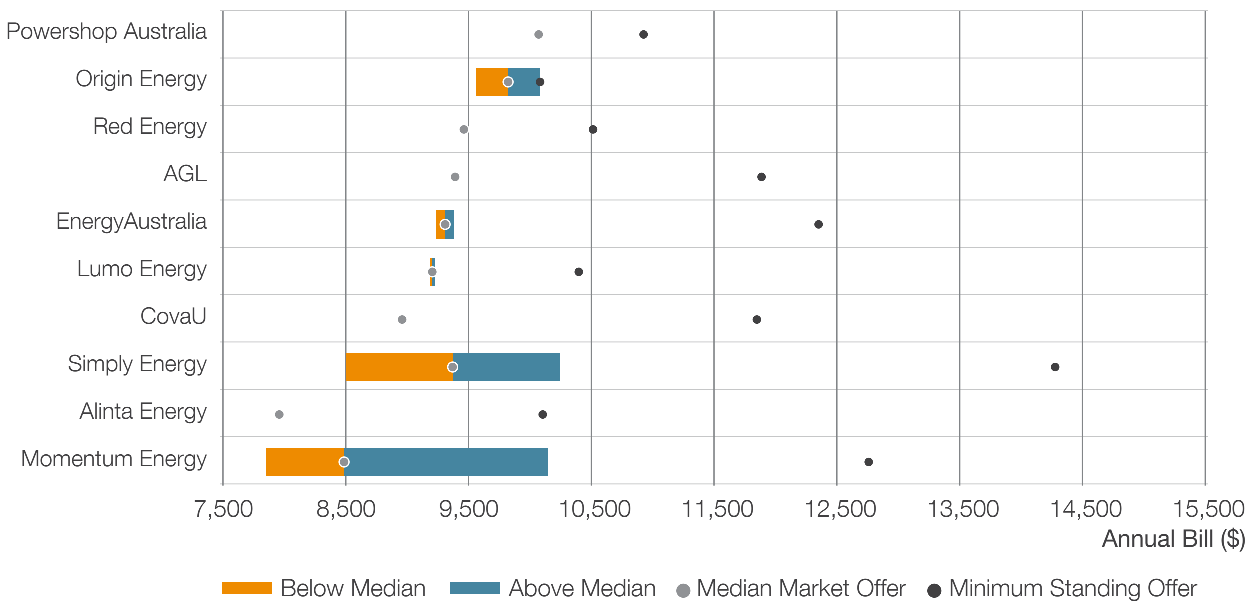


Comparison of small business market offers in 2020-21

Spread of all market offers for small business electricity by retailer, for CitiPower (12,000 kWh)



Spread of all market offers for small business gas by retailer, for Australia Gas Networks central area (500 GJ)



Customers experiencing payment difficulty

Gas

43,376
number of residential customers receiving tailored assistance on 30 June 2021

$501
average arrears of gas customers receiving assistance (can pay ongoing use)

$1,334
average arrears of gas customers receiving assistance (cannot pay ongoing use)

Electricity

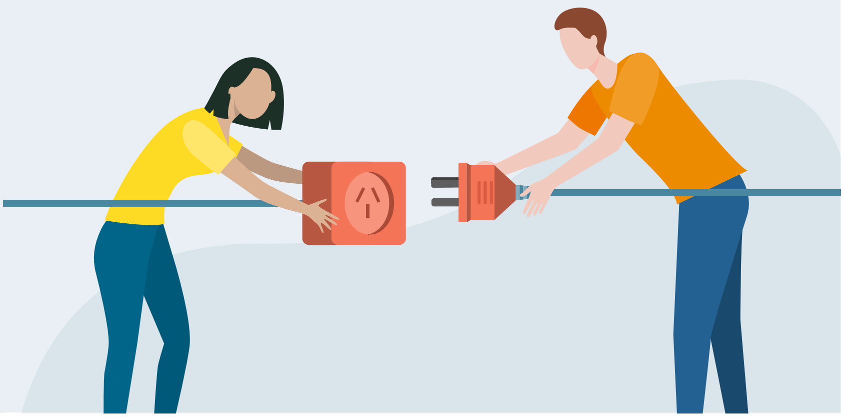
60,148
number of residential customers receiving tailored assistance on 30 June 2021

9,571
residential customers disconnected for non-payment in 2020-21 (electricity and gas)

$486,725
amount paid to customers who were wrongfully disconnected

$695
average arrears of electricity customers receiving assistance (can pay ongoing use)

$1,836
average arrears of electricity customers receiving assistance (cannot pay ongoing use)



Distributor performance

Average number of electricity interruptions in 2020

Distributors are responsible for the reliability of energy supply. Electricity distributors maintain infrastructure such as the poles and wires connecting customers' property to the grid. Distributors are required to notify customers in advance if there is a plan to shut off a customer's supply.

However, customers may experience unplanned outages from time to time. The average minutes and number of unplanned outages experienced by customers are shown in the tables below.

Figure 1 – Minutes of unplanned interruptions per customer

Distributor	2019	2020	$ change
CitiPower	37.75	27.88	-26%
Jemena	66.92	49.71	-26%
United Energy	50.32	42.93	-15%
Powercor	193.74	148.60	-23%
AusNet Services	339.13	384.58	13%

Figure 3 – Average unplanned interruptions per customer

Distributor	2019	2020	% change
CitiPower	0.418	0.387	-7%
Jemena	0.987	0.803	-19%
United Energy	0.718	0.615	-14%
Powercor	1.907	1.565	-18%
AusNet Services	2.142	2.216	3%

Guaranteed service level scheme payments to customers

We oversee a guaranteed service level scheme that requires distributors to make payments of up to $360 to individual customers when certain service levels are not met. Total payments under the scheme decreased by 9 per cent in 2020, as shown in Figure 2 below.

Figure 2 – Electricity guaranteed service level payments, total numbers and amounts by type

Reasons for payment	2019	2020
Late appointments with customers	19	173
Delay in connecting supply	1,041	1,937
Repeated or lengthy power outages (low reliability of supply)	113,398	109,555
Faulty streetlights not repaired in time	121	393
Total number of payments	**114,579**	**112,058**
Total payments	**$15,163,995**	**$13,868,415**

Unaccounted for gas

Unaccounted for gas (UAFG) refers to the difference between the measured quantity of gas entering the gas distribution system from various supply points and the gas delivered to customers. There are various causes for UAFG, including fugitive emissions, metering errors, heating value, data quality and theft. In Victoria, UAFG is managed via a benchmark process and our Gas Distribution System Code sets benchmarks for each Victorian gas distributor.

Retailers are required to purchase enough gas to cover customer consumption and the actual UAFG. Each year, gas distributors and retailers each reconcile the amount of gas purchased against UAFG benchmarks. The latest settled data for class B customers are shown in the following table and figures. There is always a lag in the most recently available data to allow for accounts to be settled. The latest completed settled data for our gas network is up to 2018, as per the table below.

Figure 4 – Class B UAFG for DTS networks, data and benchmarks

Distributor	2018–22 benchmark	UAFG (2018)
AusNet Services	4.6%	4.73% (unsettled)
Australian Gas Networks	4.0%	4.19% (unsettled)
Multinet Gas Networks	5.3%	5.35%

Only unsettled data has been provided for AusNet Services and Australian Gas Networks, as settled data was not available at the time of reporting.