



**1 April 2019**

Essential Service Commission  
Level 37, 2 Lonsdale Street  
Melbourne VIC 3000

**Re: Submission to Victorian Default Offer**

We write in response to the call for submissions in the Draft Determination of the Victorian Default Offer ('VDO') to apply 1 July 2019. WINconnect is a licenced retailer in Victoria and specialises in providing services to Embedded Networks, Microgrids and Community Energy Schemes. We are a non-vertically integrated retailer and with embedded networks we act as an energy on-seller. Whilst WINconnect operates nationally, the vast majority of our 130 staff are located in our head office in Hawthorn East, Victoria. This includes our customer service centre which is a local employer. The majority shareholding of the company is held by management within the organisation.

As a participant in the retail energy industry, we have been dismayed by obscure discounting practises and campaigns that appear to be deliberately designed to confuse consumers. It is commendable that your regulatory colleagues in the ACCC seem to be taking on these practices. We have adopted a "best tariff" offer that is typically lower than standing tariffs of the local default retailer, dispensing with pay-on-time or other conditional discounts for all customers.

WINconnect looks at the draft determination from two perspectives. We are a small authorised retailer selling electricity to on-market customers in a competitive space shared with many retailers without generation capacity. In addition to this, we also on-sell energy in behind-the-meter situations known as embedded networks. Our approach to this activity is to apply microgrid technology to position our sites as community energy networks. This includes demand management reporting, roof top solar, battery-ready infrastructure, embedded gas trigeneration facilities and high efficiency smart technologies. We invest in the assets required to deliver these sustainability benefits. An embedded network platform configured as a microgrid is the optimal means of delivering roof-top solar generated electricity to consumers within apartment buildings. Without our endeavours, individual lot owners who cannot install solar panels are at a disadvantage compared to home owners. The solar energy is a compliment to the bulk energy that we buy for the site. The aim is to ensure that cost of the bulk energy plus the amortisation of the infrastructure costs is not greater than the aggregate energy charged to the consumers inside the network. Like all small retailers without generation capacity, we are highly exposed to wholesale energy prices with little margin for error.

**Competition and Service Quality**

We acknowledge the difficulty The Commission has in undertaking the exercise of setting an accurate retail tariff; predictions are hard, especially about the future. That being said, we would like to highlight to the ESCV the risks associated with setting a tariff that is not reflective of the actual costs that some small energy companies face in reality. Whilst the policy of re-regulating retail prices is not the question of this submission, we would like to reiterate our commitment to policy reform in retail markets, embedded networks and on-selling driven by competitive market forces. In this regard, the work delivered to date via the Power of Choice - Embedded Network Manager reforms and ongoing reviews by the Australian Energy Market Commission receive our support and advocacy. Where we believe the rubber hits the road on embedded network regulatory reform is in delivering better service quality. More effective competition in embedded networks not only drives better price outcomes for consumers, but also drives higher quality. Quality outcomes in terms of a retail electricity offering can seem simple on the face of it but should not be discounted. Higher quality may include levels of customer service, independent dispute resolution, billing accuracy, timeliness and quality of presentation of billing information, customer information systems and portals.

As the VDO will be a genuine price cap on consumer tariffing in embedded networks, the ESCV needs to be confident that a tariff set too low doesn't threaten to drive compliant, high-quality and well-resourced service providers out of the market.

### **Embedded Networks and the VDO**

Whilst in the broader retail market, customers will still be able to receive value added services and different tariff structures under market contract rates above the VDO, due to the Transitional Pricing Rule in Clause 27 of the General Exemption Order 2017 ('GEO'), this will not be available to embedded network customers. We seek some clarification here as to how this is to be treated for existing embedded network customers on time of use or optional demand-based tariffs. We note this in context of a number of customers that may be on time of use tariffs that are at a discount to the existing local retail standing tariff. Transitioning those customers to a VDO referenced flat tariff on the 1 July 2019 may, depending on their consumption profile, result in an adverse outcome. Restricting an embedded network from providing such tariff structures only limits the options available to consumers who are looking to benefit from them.

We further note that embedded networks offer an opportunity for mass demand response and reduction in peak demand via the parent connection point. To achieve and drive change in demand response moving forward, embedded networks rely on having the ability to set cost reflective consumer retail and network tariffs. This is consistent with the push toward cost reflective network tariffing, nationally. The ability to drive consumer behaviour via innovation in tariffing structures and providing clear cost signals can offer efficiencies back to embedded networks – included consumers as their key stakeholder. Reverting all embedded networks to a flat regulated tariff appears to be a backward step in this regard.

In addition to this, we seek some guidance on the applicability of the pricing rule to customers consuming in excess of 40 MWh p.a. Whilst the VDO is applicable to small consumers, consuming under 40 MWh p.a., the pricing rule (to which it is referenced) appears to apply more broadly. We seek clarification to what pricing restrictions apply to consumers in the 40-160 MWh p.a. band in Victorian embedded networks and how this is to be enforced.

### **The Realities of Wholesale Costs in Embedded Networks and Retail Markets**

In the broader retail market, retailers manage their exposure to wholesale costs by hedging in financial markets. In embedded networks however, energy is on-sold and, traditionally, wholesale energy costs are fixed by C&I retail contracts at the parent meter. The ability to fix wholesale costs through this contracting arrangement is less flexible than that imagined in the Frontier Economics model. Embedded networks are more likely to fix wholesale cost exposures once every 12-24 months rather than progressively hedging forward loads every 12 months. This may eventually lead to mis-matches over time between the wholesale cost faced by embedded networks and the allowances based on forecasts by the ESCV for each VDO price period.

We note this in the context of increased price levels and volatility in wholesale cost since 2016. There is the potential that a rapid swing in prevailing wholesale market conditions may leave any particular embedded network exposed between their parent meter contract position and the wholesale allowance that factored into VDO.

Given that the introduction of the VDO sharply reduces the margin for error that embedded networks may have in managing their exposure to wholesale costs, we recommend that the ESCV closely consider how to better align their wholesale costs allowances with the realities of how embedded networks actually manage their contracting positions. The commission should also prepare itself for the possibility of embedded network financial default as a direct result of the VDO.

In addition to this, there appears to be no clear reasoning as to why the commission has adopted different methodologies based on different components of the cost stack. One specific example is with regards to modelling of wholesale energy cost being forecast based on 12 months of historical prices, whilst LRET costs are based on only 40 days.

## **A Management Plan for Orderly Exit of Retailers and Concentration**

Given the proposed level of the VDO in the draft determination, the ESCV should be prepared for potential default and eventual concentration of service provision back to tier 1 retailers.

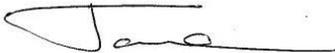
In setting a regulated VDO essentially based on cost averages, the ESCV will inevitably create winners and losers in the retail market based on where incumbent service providers are likely to sit on either side of those averages. In all likelihood some retailers, ENOs and EN service providers will be driven out of the market in Victoria as a result of the VDO. It is our view that this is likely to occur in the smaller end of the market where retailers are not vertically integrated and rely on service quality as a differentiator. The commission should prepare itself for potential default and consolidation of retailers and ENOs in Victoria. Retailer default and transfer of energy consumers back to tier 1 retailers under ROLR provisions would, without doubt, be a poor outcome for the large number of consumers who have been previously churning away from those companies under a free market.

## **Future treatment of the VDO and the Pricing Rule in the GEO**

We believe there may be real short-term risks in the initial use of the VDO as a reference point to the pricing rule in the for the period commencing 1 July 2019. It would seem prudent that the ESCV provide an indication as to whether it intends to continue of with the VDO as a reference for the GEO pricing rule beyond the transitional period or if it intends to set a separate embedded network price cap under the conditions available in section 10 the GEO. This will provide greater regulatory clarity for embedded network operators and consumers moving forward.

The centralised price fixing of any commodity in a market-based economy is necessarily courageous. The onus for revising the VDO will ultimately pass to subsequent governments. It is quite foreseeable that network costs will rise (for example, due to augmentation to better accommodate distributed renewable generation assets) and this will eventually need to be passed on through an increased VDO.

Sincerely,



James Norton

Executive General Manager – Energy Markets