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Essential Services Commission
Level 37, 2 Lonsdale Street
Melbourne, Victoria 3000

Submitted by email: retailenergyreview@esc.vic.gov.au

Victorian Default Offer to apply from 1 January 2020

Alinta Energy welcomes the opportunity to make a submission regarding the Essential Services Commission's issues paper "*Victorian Default Offer to apply from 1 January 2020* that outlines the approach and method to determine the Victorian Default Offer that will apply from 1 January 2020.

Alinta Energy is an active investor in energy markets across Australia with an owned and contracted generation portfolio of nearly 3,000MW, including 1,700MW of gas-fired generation facilities and 1,070MW of thermal generation facilities, and in excess of 1.2 million electricity and gas customers, including more than 620,000 in east coast markets. As such, we are well placed to provide comments on the Issues Paper.

Alinta Energy is concerned that the ESC's issues paper contains some ambiguous proposals which, if adopted, have the potential to undermine consumer confidence in the offers made available to them. In addition, given the ongoing energy reforms occurring at a national level, we urge the ESC to harmonise energy policy to ensure a clear message in the market is consistently being conveyed to customers.

Our further detailed comments on the Issues Paper are set out below. Should you require any additional information or wish to discuss any aspect of our submission please contact Ante Klisanin, Retail Regulation Manager on [redacted] or via email: [redacted].

Yours sincerely

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Victorian Default Offer to apply from 1 January 2020

Major changes to retail operating costs since May 2019.

As part of the ESC's advice to the Victorian Government on 3 May 2019, the *Victorian Default Offer to apply from 1 July 2019* included an allowance of approximately $3 per customer for the implementation and maintenance of the Payment Difficulty Framework (PDF). As noted in the 1 July VDO advice;

> *'Given that the benchmark data we used is unlikely to fully include these net costs, we proposed in our draft advice to include an allowance in the VDO for PDF related compliance costs at the upper end of the range adjusted for inflation.'*[1]

Alinta Energy welcome the ESC's consideration associated with PDF regulatory compliance costs but notes that a large number of significant regulatory reforms, specific to the Victorian energy market, were implemented on 1 July 2019 that should also be included in the 2020 VDO. Figure 1 below summarises the regulatory reforms implemented on 1 July 2019 and the number of business days retailers had to implement them.

Figure 1

Reform	Final Decision	No. of business days from final decision to implementation
Best offer on bill	30/10/2018	160
Clear Advice on all offers made	30/10/2018	160
GST inclusive pricing	30/10/2018	160
Advanced notification of price changes	30/10/2018	160
Customer provided meter reads	21/03/2019	65
Helping customers engage confidently in the retail energy market	21/03/2019	65
Technical final decision on Energy Fact Sheets	9/05/2019	35
Victorian Default Offer - Price determination	30/05/2019	20
Victorian Default Offer as a reference price	30/05/2019	20
Victorian Default Offer - Corrigendum to VDO	31/05/2019	19
Victorian Default Offer - consequential changes to the ERC	13/06/2019	11

Due to the significance and challenging timeframes associated with these regulatory reforms, Alinta Energy established a Project Management Team to ensure they were delivered efficiently and effectively. The project management costs associated with establishing ongoing processes and systems for the effective compliance management of the reforms in Figure 1

[1] Essential Services Commission, Victorian Default Offer to apply from 1 July 2019, 3 May 2019, p. 54

were approximately $[redacted] Alinta Energy recognises the importance of building trust in the energy market by having comparable offers that are easily understood, however the complexity associated with delivering these outcomes has resulted in an ongoing regulatory cost that has been established within retailers' processes and systems and as such should be considered as part of the 2020 VDO.

The Retailer Reliability Obligation (RRO) was yet another regulatory reform introduced from 1 July 2019. A national initiative, the RRO has been introduced to help manage the risk of declining reliability, whereby triggered RRO events will require retailers to enter into sufficient contracts to meet their share of expected system peak demand.

As part of the RRO consultation process, the Energy Security Board released a regulatory impact statement on 19 December 2018. The RRO impact statement determined compliance costs for the RRO associated with market customers and large end users would be in the range of $176 million over the next 10 years[2], These compliance costs include both operational compliance costs and physically backed contracts. Costs which should be assessed and included in determining the 2020 VDO

Alinta Energy urges the ESC to consider the cost of regulatory reforms and their impact when determining the 2020 VDO. The ESC must ensure its method is consistent with previous decisions (noting that regulatory costs of the PDF were considered in the 1 July 2019 VDO advice) and ensure that retail operating costs are not materially understated. Alinta Energy considers the most appropriate approach to quantify these costs (and ongoing compliance costs) would be in the form of the data collection approach referred to in the issues paper.

VDO compliant maximum annual bill

The issues paper outlines the approach for setting the 2020 VDO for;

i. flat,
ii. flat and controlled load, and
iii. non-flat tariffs.

Alinta Energy supports the approach to set the VDO tariffs under the same structure as the 1 July 2019 VDO advice. With the introduction of a *VDO compliant maximum annual bill* to be included for non-flat tariffs. The method used for Approach 1 & 2 is logical for flat tariffs, however the process cannot be applied as simply to non-flat tariffs. The rational to this logic is that non-flat

[2] Energy Security Board, Retailer Reliability Obligation Decision Regulation Impact Statement, 19 December 2018, p.44

tariffs costs vary based on individual usage profiles. Simply applying a consumption amount to the *VDO compliant maximum annual bill* can lead to distorted outcomes, and not deliver on the expectations of customers who are using non-flat tariffs. Alinta Energy notes that the section 13 Order in Council (the Order) specifies usage allocation, as listed below in Table 1. Although not referred to in the issues paper, we assume that this would be used to determine the *VDO compliant maximum annual bill* for non-flat tariffs.

Table 1 – Usage allocation for flexible tariffs

Tariff type	Peak	Shoulder	Off-peak
Flexible price (3 part time of use)	0.25	0.45	0.30
5-day time of use	0.52	0.00	0.48
7-day time of use (small business customers only)	0.74	0.00	0.26
5-day time of day 9 pm off peak (United Energy distribution zone only)	0.25	0.20	0.55
5-day time of day (United Energy distribution zone only)	0.32	0.20	0.48

The issues paper discusses options below for how retailers would structure their non-flat pricing offers;

1. None of the rates a retailer charges under a non-flat standing offer tariff are above the VDO flat rate, or
2. The peak rate can be above the VDO flat tariff rate, with the shoulder and off-peak rates set below the VDO flat tariff rate, or
3. Withdraw all non-flat standing offer tariffs from the market.

Option 1 would not only be commercially unviable for any retailer but would defeat the purpose of offering cost reflective non-flat offerings. In this scenario, the non-flat tariff would be the best offer for customers but would provide little incentive for customers to consume less during peak times as the peak rate for the non-flat offer is at or below the VDO flat tariff rate.

Option 3 hinders cost-reflective initiatives that retailers could develop in an energy market that is already struggling with energy reliability during peak demand periods.

Accordingly, option 2 is the only position Alinta Energy would support.
That being said, we have concerns about the representations made within the issues paper as to the application of option 2. In particular, the issues paper states;

> *Based on their understanding of their customers' usage profiles, a retailer may charge peak rates on their non-flat standing offer tariffs that are above the VDO tariffs*

The above statement implies that retailers would need to monitor their customers' usage allocation and vary their VDO non-flat tariffs accordingly, so as to not exceed the *VDO compliant maximum annual bill.* We urge the ESC to ensure that the 2020 VDO be priced with a representative customer (representative customer) in mind that has both'

a) An annual representative consumption amount and
b) A representative usage allocation.

The 2020 VDO for non-flat tariff customers is a viable option for new customers where retailers may not have access to the customer's usage amount or profile. Furthermore, Table 1 in our submission details 5 non-flat tariff offerings being considered; a customer may be best-served by any one of these tariff structures. Tailoring VDO non-flat tariffs to customers with varying usage profiles would be impractical, unfeasible and overly complicate the market.

Furthermore, it would appear that Approach 2 within the issues paper does not consider usage profile at all and only considers annual consumption amounts. The issues paper goes on to state;

> *The order also provides that (for domestic and small business standing offer customers on non-flat tariffs or any combination of a flat and non-flat tariffs) the commission may provide for how any overpayment by those customers is to be dealt with*

Alinta Energy has concerns that the ESC has not considered the importance of usage profile in determining whether or not a customer has overpaid as a result of their profile not being representative of the usage allocation applied to the *VDO compliant maximum annual bill.*

To illustrate the need for a *VDO compliant maximum annual bill* to be based on a representative customer, the worked example below in Tables 2, 3 & 4 highlight this requirement. Table 2 has been extracted from the prices set in the issues paper and is the VDO flat tariff price.

Table 2

Flat tariff customer	Usage allocation %	Usage allocation kWh	VDO tariffs	$
Anytime usage charge	100	4,000	$ 0.2464	$ 985.60
Daily supply charge			$ 1.2972	$ 473.48
Maximum annual bill				**$ 1,459.08**

Table 3 is a non-flat VDO tariff, that has been set by a retailer, using the VDO flat tariff rates and the usage allocations from Table 1. Table 3 has a peak rate above the Flat rate in Table 2, but the *VDO compliant maximum annual bill* does not exceed $1,459.08.

Table 3

5-day time of use set by retailer	Usage allocation %	Usage allocation kWh	VDO tarifs	$
Peak	52%	2080	$ 0.2800	$ 582.40
Off-peak	48%	1920	$ 0.2100	$ 403.20
Daily supply charge			$ 1.2972	$ 473.48
Maximum annual bill				**$ 1,459.08**

The non-flat VDO tariff utilises a Peak usage allocation of 52% and an off-peak usage allocation of 48%. Similar to a variance in total usage consumption, a change in the actual usage allocation (based on a customers' profile) can lead to a customer annual bill exceeding the *VDO compliant maximum annual bill* as seen in Table 4.

Table 4

Example customer	Usage allocation %	Usage allocation kWh	VDO tarifs	$
Peak	65%	2600	$ 0.2800	$ 728.00
Off-peak	35%	1400	$ 0.2100	$ 294.00
Daily supply charge			$ 1.2972	$ 473.48
Example customer annual bill				**$ 1,495.48**
Overpayment due to customers time of usage allocation				**$ 36.40**

To that end, Alinta Energy's preference is to align the non-flat VDO to the approach used by the Australian Energy Regulator's, Default Market Offer approach, utilising the usage allocation from Table 1, and establishing a framework for representative customers. As opposed to requiring retailer to develop tailored rates (based on bespoke usage profiles) which would lead to multiple offers in the market. This would also remove ambiguity in relation to possible overpayments and establish expectations in the market where customers can pay more than the *VDO compliant maximum annual bill* when they consume beyond the thresholds of a representative customer.

Embedded network customers

Alinta Energy supports the introduction of a VDO for embedded network customers, who should have the same protections as other Victorian customers. We believe the *VDO compliant maximum annual bill* to be the most appropriate method for these customers.

Alinta Energy acknowledges the operational difficulties relating to the differing embedded network configurations but would be happy to assist the ESC in determining appropriate measures.

Other matters

Alinta Energy reiterates the need to incorporate residential and small business load profiles separately segregated MRIM data that provides the relevant load shape profiles for residential customers and small business customers below 40 MWh pa. The implication of having a blended profile of all customer types up to 160MWh pa is that it does not accurately reflect the peakier profiles of the residential and small businesses (up to 40 MWh) segments, thereby significantly understating retailer hedging costs. Given the number of different profiles, we urge the ESC to adopt an appropriate volatility allowance.