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Essential Services Commission of Victoria

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Submission to Victorian Default Offer 2021 Draft Decision

Tango Energy thanks the Essential Services Commission of Victoria (ESC) for the opportunity to make this written submission on the draft decision paper on the Victorian Default Offer 2021. Tango Energy has also made written submissions on the consultation paper released in July 2020 on the Victorian Default Offer 2021, and made previous submissions on the 2019¹ and 2020² VDO prices.

Methodology for the 2021 draft decision generally builds on previous determinations, and considers departures or review of concerns with existing methodology unwarranted on the basis of decisions made during the 2019 and 2020 determinations. This applies particularly in relation to previous stakeholder concerns relating to the estimation of wholesale costs.

Tango Energy has concerns with this approach. Relevant legislation does not constrain the ESC from departing from previous methodology in future determinations, particularly where potential methodological flaws have been identified. It is disappointing that opportunities to improve and mature the VDO framework have not been utilised, particularly after 3 years of data have been collected.

In addition to our concerns reiterated in previous submissions, we would like to take this opportunity to highlight further issues specifically concerning allowances for pass through events and retailer operating costs. These are discussed in further detail in the remainder of our submission. In summary, we consider that a systematic methodology to consider the merits of including costs relating to pass-through events impacting all industry participants, e.g. costs of regulatory change, or effects of the COVID-19 pandemic, should be developed. We also make comments about the use of retail operating benchmarks.

We note recent findings of the Australian Energy Market Commission (AEMC) in its 2020 Retail Market Competition Review³, and the findings of Esplin, Davis, Rai, & Nelson (2020)⁴. There now appears to be evidence that a downward bias of the VDO level has resulted in detriment to consumers in the withdrawal of the lowest priced market offers. We continue to urge the ESC to take the interests of and impacts on all Victorian energy consumers into account.

¹ Tango Energy submission to VDO to apply from 1 July 2019, 4 April 2019:
https://www.esc.vic.gov.au/sites/default/files/documents/4_4_2019%20VDO%20draft%20advice%20submission%20Tango%20Energy%20redacted.pdf

² Tango Energy submission, Re: VDO to apply from 1 January 2020 – Draft Decision, 17 October 2019
https://www.esc.vic.gov.au/sites/default/files/documents/SBN%20-%2017_10_2019%20VDO%202020%20Draft%20Decision%20Submission%20Tango%20Energy%2020191017.pdf

³ 2020 Retail Energy Competition Review, AEMC, 30 June 2020:
https://www.aemc.gov.au/sites/default/files/documents/2020_retail_energy_competition_review_-_final_report.pdf Page xiv, point 68

⁴ Esplin, R., Davis, B., Rai, A., & Nelson, T. (2020). The impacts of price regulation on price dispersion in Australia's retail electricity markets. Energy Policy 147, 111829.

Pass-through costs – COVID19, 5MS

As the ESC is aware, the energy retail industry has, and is continuing to prepare for continuous regulatory changes with significant strategic, operational and technological impacts⁵. Costs to industry relating to the five-minute settlement (5MS) reforms have been extensively consulted on by the Australian Energy Market Commission (AEMC).

The COVID-19 pandemic has also had an impact on energy businesses operationally, through an increase in doubtful debt and lessened collection activity on missed customer payments as energy retailers provided support to customers experiencing financial difficulty due to the pandemic, including stopping disconnecting customers for non-payment from April to June⁶.

A final decision was made by the ESC on 24 August on “Supporting energy customers through the coronavirus pandemic 2020” to require retailers to provide additional assistance to customers due to the pandemic, based on leading hardship indicator information provided by retailers on a voluntary basis since April 2020 and on an ongoing basis. In making its final decision in its rule change on 24 August 2020, the ESC appears to have found clear evidence that there are indicators and data on stress on doubtful debt:

Quoted from the ESC’s Supporting energy customers through the coronavirus pandemic 2020 final decision paper:

“Based on the evidence available to us since the start of the pandemic, we consider there is a need for targeted reforms to support residential and small business customers paying their bills through the pandemic. These reforms aim to provide affected customers with consistent communication on the range of payment assistance measures available to them”

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“Missed bills, payment deferrals and average arrears Data we are receiving from retailers shows an increase in the number of both electricity and gas residential customers missing their bills during the pandemic. On average, 42,510 electricity and 30,088 gas customers missed a bill payment each week in July (across the market, not just in Victoria), compared to 38,535 electricity and 27,432 gas customers in April. We note that levels of missed bills will fluctuate between weeks depending on billing cycles, and may capture some customers who regularly miss bills and pay a few days late.”

p.35

“Although the number of small business customers receiving assistance has remained consistent, the average arrears of the small business customers that were receiving payment assistance from their electricity retailers has increased in every month since we commenced collecting this data.”

Notwithstanding, the ESC has not allowed for COVID19 pandemic costs and doubtful debts on the basis that there is insufficient information to justify any changes (p24, Draft Decision). We

⁵ AEMO Major Programs, accessed 14 Oct 2020 <https://aemo.com.au/en/initiatives/major-programs>

⁶ p8, Victorian Energy Market Update: September 2020 <https://www.esc.vic.gov.au/sites/default/files/documents/RPT%20-%20FINAL%20-%20Victorian%20Energy%20Market%20Update%20-%20September%202020.pdf>

note that the interim EY report to the ESC⁷ stated that “Overall there is a lack of information to determine whether the retail operating margin has been materially impacted by COVID-19.” Tango Energy was not requested to provide any information to this report.

This position is surprising to Tango Energy. We provide further information in the confidential appendix to this submission which shows a clear one-off increase in OPEX as a result of doubtful debt to aid the ESC in its deliberations, as requested and noted in the ESC’s public forum on 8 October 2020. We also note that publicly available Australian Stock Exchange (ASX) announcements by listed energy companies relating to doubtful debt and impact on earnings have been made^{8 9}. There is also considerable data available from the Australian Energy Market Commission from considerations in making its determination on whether to delay the implementation of Five Minute Settlements (5MS)¹⁰.

In summary, notwithstanding the observations by EY relating to increased doubtful debt impacts on retail operating margin, we do not agree that the inability of EY to determine whether the retail operating margin has been materially impacted by COVID-19 justifies the omission of these considerations in the retail operating cost stack for the 2021 VDO determination.

Benchmarking Retail Operating Costs

As per the draft decision:

p.22 “The 2021 allowance for retail operating costs per customer is based on the benchmark of \$121.07 set by the Independent Competition and Regulatory Commission in its 2017 final decision for retail electricity prices in the Australian Capital Territory.

For our draft decision (and consistent with our past approach) we adjusted this benchmark for the change in the consumer price index (CPI) since 2017 which leads to a benchmark of \$125.12.”

Tango Energy notes that since the 2017 final decision made by the ICRC, two further reviews and investigations of ICRC’s price-setting methodology for 2018-19 and 2020-24 have been undertaken. We encourage the ESC to address apparent inconsistencies between the VDO draft determination for 2021, and the ICRC’s 2020-24 final report, particularly as they relate to pass-through events.

Furthermore, there have been significant structural changes to the retail market since 2017 which may affect the relevance of 2017 data.

⁷ Impact of COVID-19 on the efficient costs for retailers to supply electricity; Interim Report Essential Services Commission, 28 August 2020 <https://www.esc.vic.gov.au/sites/default/files/documents/Effects%20of%20COVID-19%20on%20VDO%20pricing%20-%20EY%20Interim%20Report.pdf>

⁸ ASX & Media Release: AGL Results for Announcement to the Market 13 August 2020 <https://www.asx.com.au/asxpdf/20200813/pdf/441q6ivr1qf5t.pdf>

⁹ Origin Energy; 15 July 2020: <https://www.originenergy.com.au/about/investors-media/media-centre/origin-expects-to-recognise-non-cash-charges-in-fy2020.html>

¹⁰ Australian Energy Market Commission, Delayed implementation of the five minute and global settlement rules, 8 July 2020: <https://www.aemc.gov.au/sites/default/files/documents/deloitte-report-delayed-implementation-of-five-minute-and-global-settlement-rules.pdf>

Quoted from ICRC's Retail electricity price investigation 2020–24 Final report, June 2020:

p.66, 4.6 Retail operating costs

The 2020–21 retail operating costs are calculated by adjusting the 2019–20 per customer allowance of \$125.55 by the change in the CPI of 1.83 per cent. This adjustment takes the allowance per customer to \$127.84 for 2020–21.

p.77 The Commission considers that the costs associated with the AER's Statement of Expectations released in March 2020 in response to COVID-19 pandemic would be eligible to be considered as a regulatory change pass-through event¹.

Finally, Tango Energy notes that data was requested from retailers and provided to the ESC in compulsory information requests in previous VDO determinations. We recommend that either the retail benchmarking methodology be reviewed and updated, or that a Victorian retail benchmarking methodology be developed and reviewed as the ESC builds its empirical data base.

If you would like to discuss this submission, please contact me at stan@tangoenergy.com or 03 8621 6476.

Yours sincerely,

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CONFIDENTIAL APPENDIX

