14 December 2023

Essential Services Commission
Level 8, 570 Burke Street
Melbourne Victoria 3000

By e-mail: VDO@esc.vic.gov.au

Victorian Default Offer 2024-25 – Request for Comment

Alinta Energy welcomes the opportunity to respond to the Essential Services Commission's request for comment paper as part of determining the Victorian Default Offer for 2024-25.

Alinta Energy is an active investor in energy markets across Australia with an owned and contracted generation portfolio of over 3,300MW and more than one million electricity and gas customers. The VDO has a significant impact on our Victorian customers and striking the balance between protecting customers from unreasonably high standing offer prices while encouraging a competitive retail market – which ultimately is in the long-term interests of all consumers – is a risk inherent in any form of price regulation. Maintaining price regulation should not come at the risk of damaging competition and choice for Victorian consumers.

An alternative model

While we support the ESC's approach to limit changes to the method of determining the VDO, in the longer term we believe consideration of an alternative model would meet the objectives of the VDO and improve competition and outcomes for consumers. This would involve the ESC setting a maximum percentage differential between individual retailer's standing and market offer prices. For example, if the value were set by the ESC at 20%, retailers would be required to price their standing offer price no higher than 20% above any of their market offer prices. This simple method of price oversight would:

1. Eliminate the material risk of attempting to use regulation to identify an efficient price, which inevitably will be either too high or low;
2. Place competitive pressure on retailer's standing offer prices; and
3. Allow individual retailers to managing wholesale cost and other pricing risks in a manner that best matches their circumstances, their customers and their competitive strategy.

This approach would protect consumers from unreasonable prices (a retailer setting an unreasonably high standing offer price would be priced out of the competitive market) whilst retaining incentives for consumers to engage in the market (by permitting discounts in market offers of, in the above example, up to 20%).

To be clear, the ESC would still be required to set a benchmark rate to enable price comparisons across retailers, where the benchmark rate would be used as a common base to compare retailer's prices. However, this benchmark rate would no longer also perform the function of a universal standing offer. It could be calculated in several ways, for example as the median of all standing offer prices.

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We would welcome an opportunity to discuss this model with the ESC in more detail. Our subsequent comments in this submission are made on the basis that the current form of price regulation will be retained for 2024-25.

Wholesale electricity costs

In its request for comment paper, the ESC notes that ASX Energy peak swap contracts are not being traded in material volumes and therefore were not applied in determining the wholesale electricity costs for the VDO for 2023-24.

We acknowledge this and in absence of an alternative, support the ESC seeking over-the-counter prices from brokers (or retailers) as a proxy to replace peak swap contracts in the modelling of wholesale electricity costs.

Retail margin

In its 2023-24 VDO final decision, the ESC set the retail margin at 5.3% (from a draft decision of 5.7%). The justification for this and the use of benchmarking do not accurately reflect the margin necessary to support a competitive retail energy market, support innovation or genuine choice for consumers in the long term. The jurisdictions upon which the VDO retail margin is benchmarked to (outside of southeast Queensland, the Australian Capital Territory and Tasmania) do not offer customers (effective) choice of retailer, nor do retailers in those jurisdictions face the risk of cascading retailer failure. As such, benchmarking to jurisdictions with these features does not account for the higher risks present in Victoria.

New entry of itself does not support the reduction in the margin, and 2022 saw a record number of retailer failures across the NEM. Furthermore, a 5.3% return does not reflect other variables impacting retailers, including significantly higher interest rates set by the Reserve Bank.

Alinta Energy strongly recommends the ESC reconsider the retail margin for the VDO and restore it to a level more reflective of a level that would encourage investment in the retail energy sector (i.e., 5.7% – 6%).

We do not support further change to the method of calculating the retail margin.

Final decision timing

We remain of the view that finalising the VDO earlier than late May would reduce the administrative pressure and regulatory burden on retailers. The determination of network prices by the Australian Energy Regulator for the forthcoming year should take place earlier to accommodate this.

We would welcome further discussion of this response with the Commission, please contact David Calder (David.Calder@alintaenergy.com.au) in the first instance.

Yours sincerely

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