Level 33, Rialto South Tower
525 Collins Street
Melbourne, Victoria 3000
Fax +61 3 8807 1199
simplyenergy.com.au

8 October 2021

Essential Services Commission
Level 8, 570 Bourke St
Melbourne VIC 3000

[Note: Confidential information has been removed from this submission]

Lodged via EngageVictoria

Dear Commissioners,

Re: Victorian Default Offer from 1 January 2022 – draft decision

Simply Energy welcomes the opportunity to provide feedback on the Essential Services Commission's (Commission) draft decision on the Victorian Default Offer (VDO) price determination to apply from 1 January 2022.

Simply Energy is a leading energy retailer with approximately 750,000 customer accounts across Victoria, New South Wales, South Australia, Queensland and Western Australia. As a leading retailer focused on continual growth and development, Simply Energy supports the development of effective regulation to facilitate competition and positive consumer outcomes in the market.

While Simply Energy understands the reasons behind the introduction of the VDO, Simply Energy does not support price regulation in competitive markets.

It is sensible to set a six-month regulatory period with a largely unchanged methodology

Simply Energy supports the Commission's proposal to reduce the regulatory period of the 2022 VDO to six months. It is preferable to match-up the timing of network price changes and VDO periods as soon as possible.

Simply Energy is also supportive of the Commission's proposal to use largely the same methodology as it did in its 2021 VDO price determination. There has been limited evidence to justify significant changes to the current VDO methodology at this stage. With the quick turnaround between VDO price determinations in 2020, 2021 and 2022, Simply Energy would prefer that any significant changes to the VDO methodology were deferred until the 2023-24 VDO price determination. This would ensure that the Commission has the time to undertake a detailed review of the VDO methodology and run an extended consultation process with stakeholders. This would enable the Commission to properly consider the implications of any major change to the VDO methodology.

Bad debt costs continue to be a significant issue for retailers

Bad debt expenses were higher than average in 2020 and have continued to worsen in 2021. Simply Energy supported the Commission's decision to include a $6 per customer allowance in the 2021 VDO to reflect the significant increase in bad debt expenses that retailers have been facing due to the coronavirus pandemic and associated government restrictions.

The coronavirus outbreaks in Victoria throughout 2021 have demonstrated the continuing risk of the pandemic on the Victorian economy. It is not unreasonable to expect that economic activity may continue to be disrupted throughout 2022 as Victoria adjusts to the next phases of the coronavirus pandemic.

Simply Energy considers that retailers face a real risk of above-average bad debt expenses in 2022. [Note: confidential information has been removed]

Simply Energy considers that the current $6 per customer allowance is a modest inclusion in the VDO cost stack that recognises the current environment of disrupted economic activity and uncertainty. The six-month regulatory period may reduce the downside of including a bad debt cost allowance, as this allowance (of effectively $3 per customer) can be removed in the 2022-23 VDO if the threat of the pandemic and associated government restrictions have passed.

The wholesale cost allowance should be considered in the context of the total VDO cost stack

Simply Energy understands the Commission's reasoning for proposing to use a 12-month trade-weighted average wholesale price rather than adopting the six-month trade-weighted average approach suggested by several retailers. It is reasonable for the Commission to prefer maintaining consistency with its methodology in previous VDO price determinations (including for the initial six-month VDO in H2 2019). However, Simply Energy considers there is a case for the Commission to be conservative in its estimation of wholesale costs, to ensure that the total VDO cost stack will enable retailers to recover their efficient costs in H1 2022.

In its 2019 advice to the Minister for Energy, Environment and Climate Change, the Commission stated that it's advice used a 12-month trade-weighted average wholesale price because a six-month average 'would understate the cost for a retailer to serve customers'.[1] Simply Energy contends that the Commission's draft decision is inconsistent with the intent behind its 2019 advice as its proposed approach would understate the cost for a retailer to serve its customers between 1 January 2022 and 30 June 2022. The differences in the costs of supplying customers in the first and second half of a year should be a relevant consideration when the Commission uses its judgement to decide whether a six-month or 12-month average is appropriate for H1 2022.

When considering whether the VDO is 'reasonably priced', the Commission must have regard to the efficient costs of supplying the regulated goods or services.[2] In addition, the VDO pricing order provides the Commission with broad discretion to consider any relevant costs or matters when making a VDO price determination. Simply Energy urges the Commission to consider its wholesale cost estimate in the full context of the total VDO cost stack and whether its proposed methodology leads to a VDO price determination that understates the costs for a prudent retailer to serve customers in H1 2022.

Simply Energy considers that the risk to retailers from the Commission setting a VDO price too low (below efficient costs) is more significant than the potential downside to customers from a VDO that is set at a slightly more conservative level. While unlikely to occur in Victoria in H1 2022, the recent experiences in the United Kingdom provide a real-life example of the outcomes that can occur when a price cap does not respond to the actual cost changes for participants in the market.[3]

[1] Essential Services Commission 2019, Victorian Default Offer to apply from 1 July 2019: Advice to Victorian Government, 3 May, p. 25.

[2] Essential Services Commission Act 2001, section 33(3)(b)

[3] In 2021, 12 UK energy suppliers have collapsed, which has impacted over 2 million customers. Several suppliers attribute their market exit to significant increases in wholesale gas prices that could not be passed through to customers due to Ofgem's price cap. See: https://www.ofgem.gov.uk/news-and-views/blog/how-youre-protected-when-energy-firms-collapse

The proposed network cost adjustment is appropriate

Simply Energy supports the Commission's proposal to make an adjustment to network costs in the VDO cost stack to account for the delay in the implementation of the 2021 VDO variation. Network costs are a pass-through for retailers and contribute a significant proportion to the total VDO cost stack. For that reason, it is important that retailers can pass the full amount of these costs through to their customers.

Simply Energy is comfortable with the Commission's proposal to estimate under- and over-recovered amounts based on actual electricity usage in July and August 2021.

It is appropriate to introduce a ToU VDO to reflect the two-part ToU network tariffs

Simply Energy reiterates its support for the introduction of a new two-part time-of-use (ToU) VDO. The introduction of a two-part ToU VDO will simplify compliance for retailers and will also ensure that the specific VDO tariffs are transparent and consistent across all retailers.

Concluding remarks

In closing, Simply Energy looks forward to continuing to work actively with the Commission to ensure the inputs and methodology for setting the VDO accurately reflect the efficient costs of providing a retail electricity service to Victorian customers.

Simply Energy welcomes further discussion in relation to this submission. To arrange a discussion or if you have any questions please contact Matthew Giampiccolo, Senior Regulatory Adviser, at matthew.giampiccolo@simplyenergy.com.au

Yours sincerely

James Barton

James Barton
General Manager, Regulation
Simply Energy