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### **Default Market Offer Price 2020-21 Draft Determination**

Meridian Energy Australia Pty Ltd and Powershop Australia Pty Ltd (MEA Group or Powershop) thanks the Australian Energy Regulator (AER) for the opportunity to provide comments on the AER's Default Market Offer (DMO) Price 2020-21 Draft Determination (the Paper).

#### Background on the MEA Group

MEA Group is a vertically integrated generator and retailer focused entirely on renewable generation. Powershop is an innovative retailer committed to providing low prices for customers and which recognises the benefits to customers in transitioning to a more distributed and renewable-based energy system. Over the last five years, Powershop has introduced several significant, innovative and customer-centric initiatives into the Victorian market, including the first mobile app that allows customers to monitor their usage, a peer-to-peer solar trading trial and a successful customer-led demand response program.

Powershop has also been active in supporting community energy initiatives, including providing operational and market services for the community-owned Hepburn Wind Farm, supporting the Warburton hydro project, and working alongside our customers to fund a large range of community and social enterprise energy projects through our Your Community Energy program.

#### General comments

Powershop was generally supportive of the AER's carry-forward approach to the Default Market Offer 2 (DMO2), if it was implemented in a fair, cost-reflective manner. However, Powershop does not agree that the DMO2 will enable retailers to fully recover all costs incurred.

By not allowing retailers to recoup all costs incurred, the incentive to innovate and develop further mechanisms to manage the transition to renewables (e.g. demand management, electric vehicles etc) will significantly reduce. The AER encourages and expects retailers to continue the investment into innovation and development, however, sets DMO2 in a manner that will explicitly reduce the level of this innovation, for all retailers, especially Tier 2 and 3s.

#### 1. Wholesale:

As per our previous submissions, Powershop strongly advises the importance of splitting profiles into residential and business. It is disappointing that the AER chose not to split residential and small business load profiles, citing a lack of smart meter technology in the DMO areas. While, the Consultant may conclude that there are few customers with smart meters, no analysis has been done on the rate of change in the roll-out nor the associated impact on retailer's hedging strategies. In addition, this decision will reduce the incentive to provide innovative products which inherently rely upon smart meters.

This limitation, which is outside of a retailer's control, will increase retailer's customer portfolio risk. The AER should provide a further wholesale cost allowance until the ability to more accurately split and assess profiles can occur. This would be considered a reasonable cost under current circumstances. By its own admission the AER Consultant's methodology "does not differentiate by retailer size and therefore does not fully reflect the costs some smaller retailers face in managing their customer load."<sup>1</sup>

The Paper also notes "we consider our forecasting methodology considers a wide range of wholesale market scenarios to capture the degree of uncertainty faced by retailers. We do not therefore provide an additional customer load volatility allowance".<sup>2</sup> Based upon the lack of data the AER and Consultant state they have to work with, we do not believe there is evidence to support this statement. In addition, as the Paper notes the "approach does not differentiate by retailer size and therefore does not fully reflect the costs some smaller retailers face in managing their customer load", it is difficult to conclude that it meets the policy intention in reflecting reasonable costs.

2. Environmental Costs and LGCs:

Tier 2 and smaller retailers will continue to absorb higher Large-scale Generation Certificates (LGC) costs than larger retailers that are able to enter into PPAs and take advantage of other hedging strategies. This is not an acceptable position and Powershop encourage the AER to adopt a greater consideration of environmental hedging timeframes and volumes traded to estimate likely costs rather than using simplistic averages that fall into the favour of retailers who are better resourced and funded. Regardless of the 'difficulties' faced it is important that the methodology encapsulates a true cost position for retailers, not a subjective view. This has not been achieved.

3. Network costs:

Even though the network component is the largest cost component of the DMO, the AER continues to follow a methodology that severely undervalues the actual network costs a retailer will incur. The AER is cognisant of the material factors network revenue determinations present and their impact on the network cost component of the DMO. As we advised that despite the 1 May DMO deadline, there is no benefit in pursuing a forecast until there is a determination concluded for both SAPN and Energex. As the Paper notes the DMO2 is to be "set using the best available information at the time, and we do not consider it appropriate to reset the index based on historical data, nor to undertake ex-post adjustments".<sup>3</sup> The AER must then provide for an allowance to the network cost component that allows for the risk that the AER's final determination is a different to the estimated changes in annual revenue.

4. Residual costs:

Powershop reiterates that CPI adjustment to Residual risks underestimates the ongoing costs of innovation and development as we advised in our response to the AER Position Paper. Despite retailer-led investments in demand response, virtual power plants and peer to peer trading occurring, there is no evidence presented by the AER to confirm that the CPI rate adjustment would cover such costs and allow for continued innovation.

In relation to the step-change framework, the AER has solely focused on 5-minute settlement, Consumer Data Rights and Retailer Reliability Obligations (RRO). To only refer to three regulatory changes and to restrict to only major regulatory or market impacts, does not adequately reflect changes in underlying retailer compliance costs. The numerous rule changes implemented from the Australian Energy Market Commission over the 2019/20 financial year have all required resources and funds to implement, are not a true reflection of the change in residual costs that have incurred.

5. Model Annual Usage and TOU:

Powershop emphasises that the AER must continue to weigh up the incentive for simplicity and consistency, against accuracy of setting annual usage amounts which are rapidly changing, especially with continued solar uptake. In addition, it is unclear what analysis has been undertaken to determine that the assumed usage for small business is "broadly representative of a small business user".

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<sup>1</sup> AER Default Market Offer Prices 2020-21 Draft determination, February 2020, Page 35

<sup>2</sup> AER Default Market Offer Prices 2020-21 Draft determination, February 2020, Page 36

<sup>3</sup> AER Default Market Offer Prices 2020-21 Draft determination, February 2020, Page 42

The AER must regularly monitor TOU tariffs for the representative customer to ensure they reflect the flat tariff network costs. Any divergence means the DMO is immediately adjusted to ensure retailers once again do not incur varying network costs.

It is important that the AER sets the DMO at levels that allow retailers to fairly recover their costs, while allowing for competition by non-Tier 1 retailers. Whilst the DMO<sub>1</sub> had the effect of reducing the level of standing offers in market, it also effectively reduced competition and the number of offers and products that were made available to consumers. This DMO will have the adverse effect of restricting such diverse offerings even further.

The Paper does not adequately diminish the risks of lower participation, innovation or levels of competition and Powershop remain concerned that the AER position will likely further reduce market benefits for customers that could otherwise be available through greater innovation and development allowances and compensation.

If you have any queries or would like to discuss any aspect of this submission, please do not hesitate to contact me.

Yours sincerely,



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