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Dear Glenn

Retail Electricity
Standing Offer Price Methodology Review
Comments on the Draft Approach Paper

Thank you for the opportunity to provide comments on the methodology that the Office of the Tasmanian Economic Regulator (OTTER) is proposing to use for its 2021/22 price investigation and its 2022 price determination for Aurora Energy's retail electricity (standing offer) prices.

I would like to make comment on one particular aspect of your proposed methodology that is of concern. This relates to the methodology that is proposed to assess the Cost-to-Serve. This element of the standing offer price is very important to consumers. Firstly, it represents a significant component of the fixed cost of the standing offer price and secondly the provision of this component within the standing offer price reflects the service a retailer provides the consumer.

Background

At its last pricing review in 2016, OTTER determined Aurora Energy's cost-to-serve allowance for Period 1 to be $33.151 million or $138.45 per customer (Chapter 6, 2016 Standing Offer Pricing Investigation – Final Report). This equates to an allowance of 37.932 cents per day. The report states that the cost-to-serve allowance provides a revenue stream to Aurora within the standing offer price to meet its operating costs associated with:

- billing and revenue collection;
- some marketing expenses;
- providing a customer call centre (providing advice and answering customer queries);

- an appropriate allocation of corporate overheads; and
- regulatory compliance.

Given that the daily fixed charge under Tariff 93 is 105.75 cents and under Tariff 31 it is 95.193 cents, the cost-to-serve reflects a significant component (between 35.87% and 39.85%) of the fixed costs consumers face.

Central among the services provided under the cost-to-serve allowance in 2016 was the Aurora Online service which provided consumers with direct on-line access to a broard range account information.

The Proposed Approach

It is noted in your discussion paper that cost-to-serve are typically estimated using one or both of the following approaches:
- benchmarking; and/or
- retail operating cost build-up.

It is also noted that OTTER proposes to continue to use a combination of cost build-up and benchmarking for the next regulatory period.

In relation to both approaches it is important that apples to apples comparisons are undertaken with other retailers; both retailers operating within the Tasmanian market and retailers operating in interstate markets.

In the past such comparison, while difficult, was reasonably straight forward as the majority of retailers, including Aurora Energy, provided a similar level of customer service. It was also straight forward as Aurora Energy, at the time of the last determination, had no retail competition within the Tasmanian market for domestic consumers.

However, since 2016 things have changed – Aurora Energy no longer holds its monopoly position, although it remains the dominant retailer within Tasmania, and Aurora Energy has chosen to differentiate itself from other retailers operating in Australia by introducing an app for which consumers must pay if they seek direct on-line access to their account.

This app costs the consumer 11 cents per day. This charge is in addition to the cost-to-serve allowance which is built into the standing offer price already paid by consumers and reflects a premium of 29% on the existing cost incurred to cover cost-to-serve. It represents a 10.4% to 11.55% increase in the fixed costs of electricity supply.

With the closure of Aurora Online during 2020, Tasmanian consumers using Aurora Energy as their retailer no longer have direct on-line access to their account information as part of the standing offer price. In its place Aurora now offer a slower forms-based enquiry service where a customer service operator must frequently intervene to provide the consumer with information previously available via Aurora Online.

Aurora+

The app now used as the basis for Aurora+ was initially introduced as the mechanism to replace Aurora's ailing pay-as-you-go metering technology. Aurora, in moving to an app based mechanism to provide a pay-as-you-go service has taken advantage of the on-going upgrade to smart electricity meters.

In setting the price point for its pay-as-you-go product Aurora has chosen a daily rate which, while higher than the standing offer price, offers a lower price point than was previously available for those consumers seeking to better manage their energy costs and pay for their electricity in advance.

It could be argued that by moving to an app-based format for its pay-as-you-go offering Aurora Energy was double dipping by charging a premium for the service. This position is based upon the fact that pay-as-you-go offerings have:

- a minimal level of bad debts; and
- revenue is received well in advance of consumption when compared to the normal quarterly billing cycle.

These two factors, when built upon what is becoming the standard metering platform within Tasmania, mean that Aurora Energy has gained a significant benefit by moving its pay-as-you-go customers to the app based product. It has gained extra revenue of 11 cents per day from each customer and has also gained what was most probably a similar amount due to the change in revenue stream and the reduced level of bad debts. These gains have been made with a minimal change in the costs faced by Aurora Energy when compared to the standing offer prices.

Additionally, Aurora Energy would probably be experiencing significant benefits by having customers on the pay-as-you-go product as opposed to having those same customers on standing offer and then having to manage them under the YES program should they suffer financial difficulties with bill payment.

When Aurora Energy closed its Aurora Online service and replaced it with the app, which was then rebadged as Aurora+, it became the only retailer in Australia who charged for their app-based service. At the same time it also became the only retailer in Australia who moved from a on-line service offering to a forms based service offering for its standing offer customers.

The introduction of Aurora+ has also involved extensive advertising and promotion to encourage its uptake and considerable and constant reworking of its web site since Aurora Online was shut down. There has also been a need for Aurora Energy to develop and support its forms based enquiry service which has replaced Aurora Online, even though there is a web based portal, which could have been a direct replacement for Aurora Online, as part of Aurora+.

Impact of Aurora+ on Cost-to-Serve Allowance

In pricing Aurora+ at a premium of 11 cents per day above the level of the standing offer price, Aurora Energy is making an explicit statement that providing a real-time on-line service to customers adds substantially to its cost-to-serve allowance over and above the cost they incurred in offering Aurora Online within the previous cost-to-serve allowance.

Given all other retailers, including 1st Energy, offer such a service, either via an app or via a web based interface, any benchmarking of their costs will need to be discounted to reflect the premium Aurora Energy have imposed on consumers within Tasmania for the same level of service.

The alternative to this approach would be to recognize that Aurora+ does not add 11 cents per day to Aurora's costs and that it is using its dominant position within the Tasmanian electricity market to seek out increased revenue from its customers.

It could also be argued that by requiring a customer service officer to intervene in many of the enquiries made using the forms based interface offered as a replacement to Aurora Online is more costly than giving consumers direct on-line access to their account information. As such any retail operating cost build-up approach may well inflate the cost-to-serve allowance.

Either way, OTTER, when undertaking its investigations and making its determination, must make an adjustment for the decision of Aurora Energy to charge a premium for what is a standard consumer offering by other retailers, both in Tasmania and across Australia.

A Final Observation

As was noted above, the cost-to-serve allowance covers the cost of providing a customer call centre that provides advice and answers customer queries. Given the information provided by Aurora Energy on its web site it is clear that all, or nearly all, the information available to a consumer using the Aurora+ app is already available to a call centre officer on their screen.

Similarly, the information provided by the app can be obtained using the forms based system which has replaced Aurora Online. This is however an inconvenient and time consuming option for both the consumer and Aurora Energy. It would also likely add to Aurora Energy's costs as compared to providing consumers a similar level of access to their account data as provided by Aurora Online which did not require call centre staff intervention to meet the majority of queries.

In this regard the app does not represent a distinct product.

It simply represents an additional channel via which information, which has already been collected and collated as part of the range of items covered by the cost-to-serve allowance, is provided to a consumer.

Conclusion

Given the introduction of retail competition within the Tasmanian retail electricity market and the decision of Aurora Energy to both close its Aurora Online service and replace it with the fee based Aurora+ app it is clear that OTTER will have to make changes to its methodology to take account of the differences which now exist in the level of service provided to consumers via the cost-to-serve allowance.

We again thank you for the opportunity to provide comment on your proposed methodology paper.

Yours sincerely

Sue Leitch
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