17 November 2017

Baethan Mullen
General Manager, Retail Electricity Pricing Inquiry
Australian Consumer and Competition Commission
23 Marcus Clarke Street
Canberra, ACT 2600

By email: retailelectricityinquiry@accc.gov.au

Retail Electricity Pricing Inquiry – Preliminary Report

Dear Mr Mullen,

Energy Networks Australia welcomes the opportunity to respond to the Preliminary Report to the above Inquiry. As observed by the ACCC, network costs have largely fallen across jurisdictions since 2014 and this reduction has absorbed some of the large increases in other segments of the customer's retail bill. We encourage the ACCC to review 2016-17 and 2017-18 prices in more detail in the final report.

Nevertheless, our member businesses are fully aware and responsive to the ongoing concerns over affordability of electricity and continue to look at ways to deliver better outcomes for customers. Networks have a plan to reduce costs by 30% and deliver cross sector savings of $100 billion over the next 35 years. This requires, amongst other actions, a faster transition toward fairer electricity pricing across Australia. Despite broad acceptance for this plan, such a transition will not be delivered in the current market conditions and regulatory context.

The ACCC inquiry represents a significant opportunity to overcome some of the barriers to implementing our plan. Energy Networks Australia believes that forward-looking actions which contribute to lower costs over the long term and which provide investment certainty are preferred and provide better outcomes for customers to other alternatives being considered. Networks are willing to assist the ACCC to deliver such recommendations in the final report.

We provide more detail to these key points in our attached submission as well as addressing other issues raised in the Preliminary Paper. Should you have any further queries, please feel to contact Brendon Crown on (02) 6272 1515 or bcrown@energynetworks.com.au.

Yours sincerely,

Andrew Dillon
Interim CEO

Inquiry into Electricity Supply and Pricing

Response to ACCC Preliminary Report

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Overview

Energy Networks Australia welcomes this opportunity to contribute to the Australian Competition and Consumer Commission's (ACCC's) inquiry into the *Retail supply of electricity and the competitiveness of retail electricity markets in the National Electricity Market* (the Inquiry).

Energy Networks Australia is the national industry association representing the businesses operating Australia's electricity transmission and distribution, and gas distribution networks. Member businesses provide energy to virtually every household and business in Australia.

We noted in our previous submission to the Inquiry on 4 July that the Inquiry is occurring at a time of significant technological and market change in the energy sector and recent significant increases in retail and wholesale market costs. The challenge to improve affordability and fairness for customers has come at a time where Australian electricity system has experienced unprecedented transformation. In the last five years we have seen:

- a decoupling of energy consumption from economic growth
- the rise of rooftop solar PV penetration to world leading levels
- the retirement of synchronous generation and the associated challenges of maintaining system strength and resilience
- significant increases in renewable energy capacity impacting physical and financial markets as well as the operation of incumbent generation
- market uncertainty, and increasingly less predictable political, policy and regulatory environments in the National Electricity Market (NEM).

Our submission points to generally reduced costs from network businesses in recent years which have absorbed the impact of substantial increases in other parts of the bill in some jurisdictions. We also reiterate our plan to deliver substantial benefits for customers into the future. This Inquiry represents an opportunity to explore these plans and make recommendations to remove barriers to delivering better outcomes for customers.

Networks' costs have generally reduced in recent years – absorbing some of the impact of higher costs from other segments on retail bills

Recent electricity price increases and its impact on affordability are likely to be a driver for this Inquiry. The ACCC has yet to analyse the data from our member businesses and the Australian Energy Regulator which suggests network costs are flat or declining and in most jurisdictions have absorbed at least some of the impact of significant increases in other parts of the bill:

- IPART's recent review of the competitiveness of the Retail Electricity Market in NSW[1] found that network prices fell by 12% (Endeavour's network) and 35% (Essential Energy's network) in 2015-16 for residential customers. Ausgrid's 2017-18 prices for a typical residential customer were approximately 16% lower than in 2014-15.
- Energex's 2017/18 network charges for a typical residential customer represent a reduction of 10.1% from 2016/17.
- Oakley Greenwood found that in Victoria distribution network costs have been gradually reducing as a proportion of the average residential customer bill - from 42.7% of the bill in 1995 to 25.4% in 2017.
- Earlier this month, the AER announced that further reductions in the network tariff and metering charge components of Victorian customer bills (between $10-$70 per annum if fully passed through) will help to offset other factors in the market which are placing upward pressure on retail prices, such as increases in the wholesale cost of generating electricity.
- The South Australia Power Networks response to the ACCC noted that while the annual retail electricity bill for South Australian residential customers has more than doubled since 1999/2000, the distribution network component for the average customer is $5 lower over that period.[2]
- Networks prices in Tasmania decreased by an average of almost 20 per cent in 2017-18 and have significantly offset recent increases in wholesale prices.

Networks continue to look at ways to deliver better outcomes for customers

Our member businesses, in their engagement with customers, are fully aware and responsive to the ongoing concerns over affordability of electricity. Networks continue to work with customers in developing ways to improve affordability and service delivery. Some examples are outlined below:

- Energy Queensland, TasNetworks, Western Power, Essential Energy, Endeavour Energy and Ausgrid have been working with Energy Consumers Australia and City Smart on a project which explores the changing needs of residential energy consumers in the information age, and the implications for time-of-use electricity pricing. The project gives householders an opportunity to have their say so we can better understand energy consumer motivators and barriers.
- Victorian distribution networks have developed information tools which allow customers to make use of the information available from their smart meters, with functions that allow customers to view their electricity use over time and to

[1] IPART (2017) Review of the Performance and Competitiveness of the Retail Electricity Market in NSW from 1 July 2016 to 30 June 2017, Draft report October 2017, p. 2
[2] Measured in 2017/18 dollars – source SAPN submission to ACCC pricing inquiry, 29 August 2017, p1

identify ways to reduce their bills and become more energy efficient. CitiPower and Powercor have developed the *myenergy* dashboard, Jemena has its *Electricity Outlook* portal, AusNet Services has the *myHomeEnergy* portal and United Energy has the *Energy Easy* Portal.

- As part of a broader engagement program, Western Power engaged with customers through an online survey (500 customers) and series of workshops (26 customers across 3 workshops). The engagement was designed to understand customer preferences in regards to tariff design and trade-offs customers are willing make in their electricity usage.
- Horizon Power has just finished an innovative demand based pricing trial in Port Hedland with 400 customers. The trial leveraged Horizon's fleet of advanced meters and customised phone app. All customers were allocated a target number of peak units to consume during the peak period of 1pm to 8pm based on their historical consumption at this time. Analogous to a phone plan, customers could easily understand their live consumption patterns through their phone app, and adjust if they were reaching their limit. Customers were engaged through the program and made efforts to stay within their limits and shift usage. Results of the trial were so positive, Horizon Power is now working with government to establish a demonstration phase of the pricing model, *MyPower*, allowing customers in other towns to opt-in and participate.

Working with CSIRO on the Electricity Network Transformation Roadmap

Given the challenges of the sector and the need to carefully balance affordability with other customer outcomes in terms of meeting low emissions commitments, security and reliability, and fairness, Energy Networks Australia partnered with Australia's national science agency, CSIRO, to develop the *Electricity Network Transformation Roadmap* (Roadmap).

Released earlier this year, the Roadmap is an evidence-based plan detailing what needs to be done during the next decade to provide Australians with more affordable energy while meeting international commitments to reduce emissions and maintaining secure and reliable supply. It is supported by around 20 supporting documents as well as comprehensive modelling and analysis. More than 200 representatives from all parts of the energy sector contributed at over 14 workshops and webinars held as part of the public consultation process. Information on the Roadmap was viewed more than 30,000 times during the development process. Feedback on the key concepts report was received from over 30 briefings across all major capital cities and regions with more than 300 participants and through a range of formal submissions.

Networks have a plan to reduce costs by 30% and deliver cross sector savings of $100 billion over the next 35 years

The Roadmap explains the milestones and actions required by the sector which have the potential to achieve significant customer savings of approximately $414 per annum by 2050. These actions co-optimise Australia's energy system and deliver efficiencies in the distribution, off grid and connected on site generation sectors, resulting in $101 billion reduction in cumulative total expenditure across the electricity sector by 2050.

In addition to greater affordability, the Roadmap identifies other opportunities from harnessing a transformed energy system:

- Customers, not utilities, will make more than $200 billion of all energy system investment decisions between now and 2050. Up to 10 million households and small customers will have onsite resources like solar, storage, smart homes and electric vehicles by 2050.
- Over 35 per cent of all electricity will be generated and managed by customers by 2050, through rooftop solar and battery storage, which can then be fed back into the grid.
- Networks could buy grid support from millions of customers with solar, storage, smart homes or in demand response programs, with annual payments worth $1.1 billion within 10 years.
- The grid therefore becomes a platform more like the internet, where customers can trade and share energy or receive payments from networks in lieu of investment in more network, with the confidence of a secure, affordable and low carbon service.

Importantly however, these benefits are reliant on:

- frameworks where customers or aggregators are given efficient incentives to provide flexible capacity services through Distributed Energy Resources (DER) 'in the right place, at the right time'
- networks effectively providing more efficient price signals to retailers through restructured network tariffs which are important for efficiency and fairness
- regulatory arrangements, which are appropriately flexible to allow network innovation and the development of shared experience.

The ACCC inquiry represents a significant opportunity to overcome some of the barriers to implementing our plan

We agree with the Commission's conclusions[3] that tariffs which largely link charges to a customers' anytime energy usage:

- provide no price signal for customers at times of the day where constraints are likely to occur leading to future network investment
- instead provide the wrong signal to avoid energy use at times which have little impact on future network costs.

Most stakeholders recognise that failure to act more urgently serves to make the problem of energy affordability worse. The Roadmap points to a critical path dependency, where benefits can only be delivered if the 'noise' from inefficient signals in current anytime volumetric network tariffs is addressed. Anytime volumetric signals incentivise investment in distributed generation for those who can afford it, regardless of location or use, and this has the unintended effect of shifting system costs onto other users without Distributed Energy Resources.

Unless this is addressed with some urgency:

- targeted incentives for the use of customer-owned rooftop solar and battery storage in the 'right place at the right time' to avoid network expenditure will be unviable or less economic
- without appropriate incentives and system operations, the rapid deployment of customer owned generation systems is likely to increase costs or threaten reliable supply of energy because of the significant potential for overload and/or breach of technical constraints on the distribution network.

To the extent that poorly designed market frameworks or government interventions limit timely progress on tariff reform, the risks will impact most directly on customers.

In order to deliver more efficient outcomes and improve affordability, networks need to assign tariffs to retailers which provide signals which can be efficiently passed on to customers with appropriate support measures and safeguards, or managed across the retailer's portfolio to ensure fair outcomes. This in turn requires positive action to increase the penetration of digital (smart) meters, and removal of barriers so that customers can be transitioned to cost reflective tariffs by 2020.

The need for more urgent transition to more efficient networks tariffs has acceptance by COAG Energy Council, the AEMC, AER as well as customer groups and retailers. Despite this, the transition away from legacy volumetric network tariffs has been virtually non-existent in most jurisdictions. The ACCC Inquiry presents a substantial opportunity to deliver meaningful actions which can drive more efficiency in

[3] Preliminary Report, page 114

electricity prices and deliver substantial long term affordability and equity benefits to customers over the long term.

The penetration of advanced meters is a critical prerequisite.

Smart meters are essential to transitioning toward better pricing and incentive arrangements. Power of Choice recommendations will ensure a steady migration towards smart meters over the next 15-20 years through new and replaced metering arrangements. However a program which only targets new connections and replacement will be inadequate to deliver the benefits identified through the Roadmap.

A quick transition is therefore dependant on market led metering deployments being successful in achieving significant meter deployment before 2021. The Roadmap recommends active monitoring of market outcomes following the introduction of contestable metering to ensure market-led deployments are effective.

Nevertheless, the experience in Victoria demonstrates high levels of advanced meter penetration on their own is not sufficient. Governments must act to ensure networks can apply more efficient network tariff structures through to retailers. Otherwise these meters will remain unutilised for cost reflective tariffs.

Barriers to cost reflective network tariffs being provided to electricity retailers must be identified and removed

Benefits from new pricing approaches are only likely to be achieved through more co-ordinated efforts across the sector including networks retailers and governments. This includes regulatory and market frameworks that incentivise higher take up of pricing arrangements that are underpinned by efficient network pricing structures.

However, as we noted in our previous submission, the current regulatory and competitive market context will not deliver the necessary transition to cost reflective tariffs via opt-in approaches.

In Victoria - the only state with substantial penetration of smart meters - a Government Order In Council mandates that networks must comply with the retailer assignment of the customer to a legacy tariff. Because of this, customer take up of cost-reflective tariffs depends on retailer willingness to convince customers to “opt in” to a cost reflective tariff.

There is also little evidence that retailers are actively marketing more cost-reflective network charges. In fact, members are reporting that discounting approaches adopted by some retailers make cost reflective tariffs less attractive compared to anytime volume rates. There is also market evidence that the segmented market strategies of retailers actively exploit the reality that many customers do not, or cannot, engage with retail offers, new services or opportunities to take up distributed energy resources.

Energy Networks Australia understands that Governments may want to retain an ‘opt in’ model in which end use customers must actively choose to enter into retail market

offers reflecting cost-reflective network tariffs. There is no continuing reason why Governments should achieve this outcome by imposing regulatory requirements with the aim of allowing the Retailer to choose to avoid cost reflective network charges. Retailers manage the cost-reflective signals of wholesale energy markets and other Cost of Goods Sold and are well positioned to manage a portfolio of input costs, add value through economies of scope and scale, and repackage energy services in tailored products to end use customers.

We recommend the ACCC review options which would still provide customers choice and control and provide Government's some certainty around customer protections but which need not impact the ability of the network to provide a cost reflective network charge to the retailer.

Ensuring that storage and other demand management options are available

We note the ACCC's interest in promoting storage and demand management options. Our concern is that current Rules and regulations are not keeping pace with changing energy and customer needs which will mean opportunities for customer benefits over the long term are foregone.

For example the AEMC recent draft determination on contestability on energy services may see customers, in some circumstances, ask to pay an increased price for competition goals because of asset-based restrictions. At a time of critical customer focus on all aspects of energy charges, the regime proposed knowingly exposes customers to higher costs, without having identified a definable benefit.

Western Power's recent proposal to change the National Electricity Rules in order to allow it to invest in a lower cost off-grid supply solution that may better meet customers' needs has been rejected by the AEMC on the basis that it is inconsistent with the National Electricity Law.

Forward-looking actions which contribute to lower costs and provide investment certainty are preferred

Energy Networks Australia supports ACCC's further investigation of options for faster uptake of both smart meter infrastructure and cost reflective tariffs. These initiatives are "no regrets actions" which deliver better outcomes for customers over the long term. These initiatives are preferred to other options put forward by the ACCC to reduce networks costs.

The ACCC proposes to examine ways to reduce the existing costs embedded in the system, suggesting write-downs of asset values may be appropriate where it can be determined that over-investment has occurred or where assets have become stranded. However this will not solve the problems that are currently causing electricity prices to increase.

As we noted earlier, network costs are generally falling and networks have plans to improve affordability by reducing network costs over the long term. Asset write-downs produce the worst outcomes for customers. Actions to reduce investment certainty have the potential to increase costs over the longer term and make affordability worse, not better.

Because network investments have long asset lives and networks are able to attract financing at relatively low rates, this keeps annual costs for customers low. This is a core design component and objective of the current regulatory regime. Recommendations which would affect the cost of financing for these investments has the potential to deliver poor price outcomes for customers.

Many of the drivers of historic cost increases no longer exist

It is widely recognised that the outlook for network costs has moderated in the last few years due to changes in these same factors, with:

- an outlook of flat or declining peak electricity demand in many locations
- the reform of State Government reliability standards in key jurisdictions to correct the prescriptive features introduced in the 2000s as well as a significant number of reforms that have been made which are all altering the investment environment for networks
- improved financial market conditions and reform of cost of debt methodologies in the AER regulatory determinations to reduce the exposure to temporal volatility.

Risks in observing periodic trends and relying on historic information

The conclusions reached in the preliminary report do not reflect the material and pressing effect of the upheaval that has occurred in the wholesale electricity market throughout 2017. The analysis also does not capture recent reversals in network price trends, some already delivered, some locked in through the latest round of revenue determinations.

The drivers of costs would have been substantially different for instance if the comparison period was a 5 year period to 2018. Even one additional year of data has a material effect. Average residential bills increased by around 30 per cent (on a dollars per customer basis) between 2007-08 and 2015-16. The inclusion of projected wholesale cost increases adds to the impact on results in residential bills increasing in real terms by 44 per cent between 2007-08 and 2016-17.

The time period chosen and the lack of current information for 2016-17 and 2017-18 are therefore influential in the ACCC's Preliminary findings and we look forward to updated analysis in the final report.

Network costs aggregated while other costs disaggregated

The ACCC analysis presents network costs as an aggregated amount, while separating out costs of retail and wholesale market elements. For example, the ACCC disaggregates the retail portion of the bill (31%) into components of margin, retail other and environmental costs. However, no disaggregation is made in respect of networks into the various elements of transmission, distribution and policy costs. Once appropriate disaggregation of network costs are made, Oakley Greenwood found that distribution costs represented only 26.4% of the average Victorian retail bill[4].

Networks are willing to assist the ACCC to deliver such recommendations in the final report

Energy Networks Australia supports an empirical assessment of drivers on cost factors impacting wholesale market increases and retail market outcomes for customers as transparent information is often difficult to obtain.

We understand the ACCC will continue to analyse the data for its final report in June 2018, and we expect the results presented will change in the final report with the benefit of the most up to date information.

Energy Networks Australia understands some members are finding inconsistencies in the network costs that are represented. While some of the information provided by retailers would be confidential, our members would appreciate the opportunity to review and reconcile retailer data with our own.

[4] Oakley Greenwood, Causes of residential electricity bill changes in Victoria, 1995 to 2017, p25