Mr Drew Butterworth
Director
Australian Energy Market Commission
Level 15, 60 Castlereagh Street
Sydney NSW 2000

Submitted online

18 September 2024

Dear Mr Butterworth,

Accelerating Smart Meter Deployment Directions Paper

The Australian Energy Council ('AEC') welcomes the opportunity to make a submission to the Australian Energy Market Commission's ('AEMC') *Accelerating Smart Meter Deployment Directions Paper Consultation* ('Directions Paper').

The AEC is the peak industry body for electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. AEC members generate and sell energy to over 10 million homes and businesses and are major investors in renewable energy generation. The AEC supports reaching net-zero by 2050 as well as a 55 per cent emissions reduction target by 2035 and is committed to delivering the energy transition for the benefit of consumers.

The AEC's central objection to the proposed consumer safeguard in the Directions Paper that retailers should not be allowed to move customers onto pricing that directly reflects the more complex network tariffs without explicit informed consent is that this would result in poor consumer outcomes. As it currently stands, the AEMC's safeguard provides a perverse outcome for up to the 50% of consumers who are worse off under a cost reflective tariff and who do not want a cost reflective tariff but would ultimately likely end up with a higher overall bill under the AEMC's proposal. The AEC does not understand any way that this can be considered in the long term interests of consumers. **It is clear to the AEC that some consumers are expressing a clear wish not to be exposed to cost reflective tariffs and the obvious answer to this is to prevent networks from reassigning customers to these network tariffs for a period following installation of a smart meter until a customer can obtain data which would inform their choice about what tariff best suits their needs.**

As we note in this submission, the AEC agrees that some customers face higher than expected bills after being placed on a new cost-reflective tariff structure. That is why the AEC finds it difficult to understand that the AEMC may be prepared to make a decision which it says "may lead to an increase in retail price levels."[1] It appears to be an incredibly perverse outcome if a customer does not want a cost reflective tariff that the regulatory outcome is for them to be placed on a tariff which will result in them paying a higher price – particularly when other options such as a pause on network tariff reassignments are available.

Background

In 2014, following a rule change request from Energy Ministers, the AEMC changed the rules regarding how Distribution Network Service Providers ('networks') structure their pricing to consumers. The new rules required networks "to develop prices that better reflect the costs of providing services to individual

[1] AEMC (2024) op cit p.10

Level 13, 575 Bourke Street
Melbourne 3000
GPO Box 1823 Melbourne Victoria 3001

P +61 3 9205 3100
E info@energycouncil.com.au
W energycouncil.com.au

ABN 926 084 953 07

consumers so that they can make more informed decisions about how they use electricity."[2] To implement this objective, networks were required to "develop price structures that are reasonably capable of being understood by consumers and allow network businesses to manage the impacts on consumers of price changes by gradually moving to new network prices over several years."[3]

Whilst the AEMC noted retailers operating in a competitive market should not be required to price their offers in a way which matches the structure of the network tariff, it did note that "because network charges are retailers' largest cost, they will have a significant incentive to pass on network price signals to consumers in some form when deciding how to structure their retail prices."[4] Despite this opportunity not to pass through the tariff structure, the AEMC was very clear that its intent was for consumers to see the impact of their usage on their electricity bills:

> "Each network tariff must be based on the long run marginal cost of providing the service. Long run marginal cost is a measure that includes the future network costs that are incurred by using more energy, or the costs that could be saved by using less energy. Using this measure as the starting point for calculating network prices means that prices will allow consumers to compare the value they place on using the network with the costs of doing so."[5]

So, what has changed in the decade since this decision and why are we now concerned about retailers passing through network price signals to end users? In short, it is because more customers are starting to see more complex electricity prices on their bills as the smart metering rollout gathers steam. And as an adjunct, some are highlighting the impact and their concerns about what they pay through the media. With a smart meter an enabler for pricing reform, complex pricing has been conflated with the smart meter rollout, putting pressure on regulators and Governments to try to separate the two reforms.

In the Directions Paper, the AEMC has proposed to derisk the customer outcomes of the smart meter rollout, which they are keen to fast track, by suggesting retailers should not be allowed to move customers onto pricing that directly reflects the more complex network tariffs without explicit informed consent ('EIC'). The AEMC also proposes that some retailers should be required to offer a flat tariff to any customer that wants one. While the proposal seems to be contrary to the AEMC's own pricing principles developed in 2014, more importantly, it will likely drive-up prices overall by placing regulatory risks on a party unable to efficiently mitigate them, i.e. the retailer. To consider the impact of these new regulations, an assessment of the likely outcome on affected parties is necessary.

The driver in this scenario is the AEMC's decision that all customers must have a smart meter installed by 2030. The practical impact of this is that what was originally proposed as a market-led smart meter rollout where retailers would install smart meters where their customers could derive value from their installation and reduce their costs, is transitioning into a mandated regulatory rollout to every customer. In this new environment, retailers will now be required to install smart meters just to meet the 2030 deadline, regardless of the apparent customer benefit.

This change in approach came out of a three-year review into metering arrangements completed by the AEMC in 2023. Interestingly, that review did not recommend that any additional pricing protections for customers following the installation of a smart meter was required, other than for the provision of clear information to be provided to the customer.

---

[2] AEMC (2014) Distribution Network Pricing Arrangements, Final Determination at https://www.aemc.gov.au/rule-changes/distribution-network-pricing-arrangements#:~:text=Overview,about%20their%20use%20of%20electricity p.i

[3] AEMC (2014) ibid p.i

[4] AEMC (2014) op cit p.viii

[5] AEMC (2014) op cit p.iii

Level 13, 575 Bourke Street
Melbourne 3000
GPO Box 1823 Melbourne Victoria 3001

P +61 3 9205 3100
E info@energycouncil.com.au
W energycouncil.com.au

ABN 926 084 953 07

In March 2024, three market participants submitted a rule change intended to implement the recommendations of that smart meter review. In its April 2024 Draft Determination, the AEMC initially proposed to require retailers to provide customers with 30 business days' notice of a change to their pricing structure, as opposed to the existing five business days. In the Directions Paper issued in August 2024, the AEMC has indicated a preference that the consumer safeguards be further strengthened, to limit the ability of retailers to pass on pricing that directly reflects the network pricing structure changes except in certain circumstances.

The outcome of this proposal is that energy retailers will be billed by the network for a highly complex and often volatile pricing structure, but the structure of the price they will bill customers will be limited to either a flat tariff, or a more complex tariff if they obtain EIC. It seems likely that such a mismatch would increase the risk retailers face in pricing their products, likely driving up prices overall. This outcome was flagged both by the AEMC in 2014 when it made clear that a retailer who did not pass through network price signals in some form would face significant risks, and more recently in the Directions Paper, when it noted network and retail costs would likely be higher due to fewer customers being exposed to cost reflective pricing than they would otherwise, and retailers likely increasing their prices to manage the additional risks.

For consumers, a more complex network tariff that is passed through directly by the retailer moves pricing risks from the network and retailer to the customer. Whilst the 2014 AEMC decision said that individual customers are the party most able to manage their own consumption patterns and therefore their pricing outcomes, they importantly tempered that expectation by requiring that the network pricing structure faced by the consumer needed to be "reasonably capable of being understood by consumers"[6] and "Consumers will not be able to respond to the price signals that network prices are intended to send if they cannot relate their usage decisions to the price structure."[7] From the AEC's perspective, a demand tariff or other highly complex tariffs, clearly fail this requirement because they are not reasonably capable of being understood by a customer, nor easily relate their usage decisions to the price structure. This is especially true of demand tariffs, where consumers find out well in arrears of any demand reset.

Retailers vision for tariffs

There is an important distinction which needs to be made between network tariffs and retail tariffs. At present, the drive for cost reflectivity is at the network end, with networks developing network tariffs which are then approved by the Australian Energy Regulator ('AER').

The AER states that network tariff reform is important to reduce the need for additional investment and reduce the amount of network infrastructure that needs to be maintained. However, this requires that the customer receives the signal of the cost reflective network tariff and changes their behaviour based on this signal. Price signals can also be responded to by third parties on behalf of customers, rather than the customers themselves, and this concept may inform the AER's rationale. However, recent moves towards regulating retailer behaviour on tariffs and retail price regulation are taking away the tools needed by third parties to respond in this manner.

Businesses have been managing cost reflective network tariffs for several years while the wide scale introduction of residential cost reflective tariffs has only started to occur over the last two years. And just like the business customers before them, a significant proportion of residential customers who are faced with a network tariff which is passed through to them by their retailer have complained about their new tariff and found it impossible to relate to.

[6] AEMC (2014) op cit p.i

[7] AEMC (2014) op cit p.9

Opt in to innovation – a better customer experience
Complex network tariffs should not be mandated for customers – they should be opt in. Research reveals that active consideration of a complex electricity tariff is likely to be limited to a very small proportion of the consumer population. Among the still smaller proportion who accept a complex tariff, their preference is an associated scheme such as automation that offers risk relief.

As the Energy Consumers Australia ('ECA') Report *Industry perspectives on electricity tariffs and retail pricing* succinctly puts it:

> "A consumer-focussed solution to pricing reform will be required to ensure all consumers are willing participants in the transition and to ensure that no consumers are left behind, Such a solution will recognize that load flexibility is not all of the people, all of the time, for all of their load, but rather some of the people, some of the time, for some of their load."[8]

Opting in to innovation meets the needs of load flexibility, without sending the majority of consumers unrelatable price signals, and punishing them with costs that they could not avoid.

Customers must be able to choose their own future
In an electrified economy, choice is important for customers so that they can find the right products and services that best meet their unique situation. Right now, demand tariffs that measure customer peak that is not a function of system peak are being imposed on customers not sought by them (or retailers) in *some* distribution networks but not in others.

As the numbers of customers allocated to these network tariffs expands, many retailers are unable to mitigate this growth in network risk (nor should have it thrust upon them) via a portfolio approach (unlike energy risk) and so over time retailers are moving to share the network price risk with the customer in a pass-through type approach.

Should customers see the network cost reflective tariff?
Under current arrangements and considering retail price regulation, it is challenging to understand the rationale for cost reflective network tariffs if customers do not see them. The benefits the AER talks about in terms of reducing the need for additional investment only accrue when customers shift their behaviour at the right scale, at the correct location, at the right time and at lower cost than other network options. Postage stamped network price signals deliver no benefits given that network utilisation differs significantly by location.

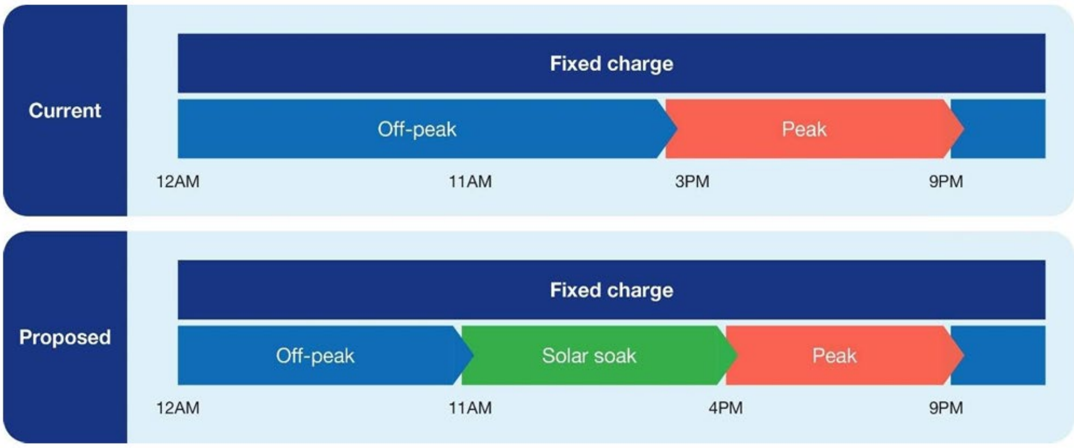
In recent months, there has been significant media attention on the challenges which customers face when dealing with cost reflective network tariffs which are passed through to customers by their retailer. There has been a reaction from decision makers to try to strengthen the consumer protections surrounding this arrangement.

The AEC position on tariffs is:

- Customers should be able to opt in to change in network tariffs in conjunction with their retailer i.e. they should not be mandated by a network that bears no obligation for education, assistance or relief.
- Customers want tariffs that are *simple* (easy to understand) and *actionable* (provide a clear price signal that they can easily act on). A key component here is that the customer both understands their retail tariff and can act on it.

[8] Energy Consumers Australia (2024) Industry perspectives on electricity tariffs and retail pricing at https://energyconsumersaustralia.com.au/publications/industry-perspectives-on-electricity-tariffs-and-retail-pricing p.3

- The AEC does not support demand tariffs or power factor tariffs for small customer classes. The AEMC is undertaking its review on Electricity pricing for a consumer-driven future, and we urge that mandatory assignment to these types of network tariffs be paused until after this more comprehensive review.
- Monitoring by the ACCC of demand retail tariff outcomes for customers shows overall comparable price outcomes for customers but not evidence that they achieve network objectives.
- The introduction of flat tariff structures with the DMO/VDO was linked to a significant reduction in innovative/complex tariffs offered by retailers. There is evidence of this up to 2021-22 but this needs to be further reviewed.
- The AEC supports simple time of use tariffs which nudge the customer towards future behaviour shifts e.g. the draft Victorian networks simple three part Time of Use tariffs developed jointly to apply across Victoria for the current round of networks TSS's.



Jemena current and proposed residential Time of Use tariff structure and timing (proposed by Victorian networks)

Source: Jemena Electricity Networks 2026-31 Draft Plan August 2024 at https://gridtalk.com.au/DraftPlan p.119

- Retailers have variously reacted to facing a larger volume of cost reflective network tariffs, with some retailers passing them through to customers and others opting not to. Retailers have different capacities to respond to the risk of these cost reflective network tariffs and ensure that the network costs incurred by customers are recovered through the retail price.
- Where a retailer opts not to pass on a cost reflective network tariff, they face the dilemma of how else to recover the cost of that network tariff from a class or classes of customer. In the wholesale market, retailers are able to manage the risk of wholesale prices through the contract and derivatives markets. There are no similar products on the network side. Network tariffs result in a cost to retailers which they must recover from their customers. If the retailer is opting not to directly pass on a cost reflective tariff shape, their choices may include smoothing out the cost over their wider customer base or retaining the affected customers on a flat tariff. Such arrangements mean either the total customer base absorbs that cost, or the individual affected customer. In the case of the individual affected customer costs being reflected in a flat tariff, a perverse regulatory outcome of a retailer not passing through a cost reflective tariff shape, is the customer paying overall higher prices. Decision makers need to address the question of how a cost reflective network tariff can be managed by a retailer in terms of risk, without the customer being adversely affected, whether it is by tariff design or overall prices.

Level 13, 575 Bourke Street
Melbourne 3000
GPO Box 1823 Melbourne Victoria 3001

P +61 3 9205 3100
E info@energycouncil.com.au
W energycouncil.com.au

ABN 926 084 953 07

- Retailers do not act to change tariffs unilaterally. Networks develop the network tariffs, and the AER approves them. Where retailers do pass on a cost reflective network tariff as a pass through, they do so as a way of managing network tariff risk.
- As the energy market evolves, retailers need industry, government, and regulator support to develop more dynamic network pricing signals to unlock the long-term benefits of the changing energy landscape for customers. EnergyAustralia is actively collaborating with the Energy Charter to try and make this vision a reality for customers. The AEC supports the EnergyAustralia collaboration.

AEMC Position in Directions Paper and AEC response

The AEMC acknowledges that some customers may be worse off after being moved to a cost reflective tariff. They say that some customers are unwilling or unable to move their consumption to take advantage of the new tariff and that these customers may experience "bill shock" and their previous flat rate plan may have been more advantageous for them.[9] The AEC notes that retailers experience the same outcome as customers when a cost reflective network tariff is passed on to them – i.e. in the same way that there are additional costs for some customers which become more challenging to manage, there are also additional retailer costs that cannot be managed in the same way as a flat tariff. Information from AEC members indicates that the move to cost reflective network tariffs has seen around 50% of customers worse off as it has flowed through to their retail bill.

The AEMC notes that the AER and joint Energy and Water Ombudsman submissions advised that retail tariff variations are a key driver of recent customer complaints, which include:

1. "being placed on a new cost-reflective tariff structure without the ability to opt out
2. customers with smart meters not being able to access a flat retail tariff offer
3. inadequate notification before a retail tariff change
4. not receiving sufficient information about the impact or implication of such changes
5. higher than expected bills after being placed on a new cost-reflective tariff structure."[10]

The AEC notes that it is unhelpful to characterise this as retail tariff variations when the underlying cause of this is a network tariff variation i.e. the retailer is just seeking to recover the cost of an underlying cost reflective network tariff. The AEC addresses each of the above five listed points below.

1. For a customer who is unable to opt out, this is usually because the underlying network tariff is mandatorily assigned, and the retailer can not opt out of it. The AEC does not support mandatory network tariffs.
2. The AEC has undertaken a review of offers in South Australia where there is a mandatory time of use ('TOU') residential network tariff for new and replacement meters. We have found that larger retailers are generally able to also offer customers the ability to opt back in to a flat retail offer, but medium and small retailers are significantly challenged by an underlying TOU network tariff.
3. The AEC agrees that some customers have received inadequate notification before a retail tariff change and that as the AEMC and AER have acknowledged, the explanation of how rule 46(4C) of the NERR would operate in the relevant AEMC Final Determination differs from the rule provision which has been a source of some confusion. The AEC welcomes clarification of the position in the Directions Paper.
4. The AEC agrees that some customers have not been receiving sufficient information about the impact or implication of changes to a cost reflective tariff. The AEC does not support demand or power factor tariffs as they are not easily explicable to customers and networks should cease assigning these types of tariffs to small customers. The AEC considers that a more simple time of use tariff can be more readily explained and could be a helpful nudge

[9] AEMC (2024) Directions Paper
[10] AEMC (2024) op cit p.ii

for some customers. In this context, the AEC supports a moratorium on network tariff reassignments until a full review has been undertaken so that sufficient consideration can be given to what tariffs customers should be exposed to and the nature of the information they require.

5. The AEC agrees that some customers face higher than expected bills after being placed on a new cost-reflective tariff structure. That is why the AEC finds it difficult to understand that the AEMC may be prepared to make a decision which it says "may lead to an increase in retail price levels."[11] It appears to be an incredibly perverse outcome if a customer does not want a cost reflective tariff that the regulatory outcome is for them to be placed on a tariff which will result in them paying a higher price – particularly when other options such as a pause on network tariff reassignments are available.

The AEC understands that the Commission can only make a rule if it is satisfied that the rule will or is likely to contribute to the achievement of the relevant energy objectives. For the Accelerating smart meter deployment rule change project, the AEMC states that the relevant energy objectives are the NEO and the NERO.[12]

The NEO is:

> to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to—
>
> (a) price, quality, safety, reliability and security of supply of electricity[13]

The NERO is:

> to promote efficient investment in, and efficient operation and use of, energy services for the long term interests of consumers of energy with respect to—
>
> (a) price, safety, reliability and security of supply of energy[14]

The AEC contends that the proposed rule does not satisfy the NEO or NERO in terms of the price outcomes likely to be delivered.

Elsewhere in the Directions Paper, the AEMC states that:

> "We do not consider that this Accelerating smart meter deployment rule change process is the appropriate vehicle to holistically consider broader reforms to network pricing arrangements. There are two primary reasons for this:
>
> 1. changing DNSPs' tariff reassignment policies would conflict with decisions made by the AER on DNSPs' Tariff Structure Statements ('TSS')
> 2. reforming network tariff arrangements through this rule change process would require detailed work and comprehensive consultation, risking delays to the accelerated smart meter rollout and the corresponding benefits to customers of accessing smart meters sooner. We also consider that these broader issues are better considered through alternate processes currently underway"[15]

The AEC considers that a pause on network tariff reassignment is a short term measure to allow for holistic consideration of broader reforms as part of the Electricity pricing review. As we have outlined in this submission, there has been a growing customer concern around tariffs and the AER would not have been fully aware of this concern until more recently. It is entirely appropriate now that the concern has been identified to pause network tariff reassignments.

---

[11] AEMC (2024) op cit p.10
[12] Section 88 of the NEL /236 of the NERL
[13] Section 7 of the NEL
[14] Section 13 of the NERL
[15] AEMC (2024)

The AEC will continue to contend that any limitation on a retailer's ability to pass through a network pricing structure should be mirrored with an identical limitation on a network's ability to mandate such a structure to retailers. Opponents will likely argue a change of this nature would come at a cost, but such claims need to be considered against a base case of the likely outcome of the AEMC's alternative rule signalled in the Directions Paper – not the AEMC's 2014 rule change. So, what will these arguments likely be, and how would they compare to the alternative of retailers alone bearing network pricing risk?

While the jury is out on its effectiveness[16], it has been said that not exposing retailers to a cost reflective tariff will mean customers are less likely to use the network efficiently and increase the total system costs by forcing new network build, the likely impact of the AEMC's proposed limitation on tariff changes will result in the same ultimate outcome as the status quo. It is unlikely that a customer with a usage pattern that is driving up network costs would change their consumption patterns if they did not see cost reflective pricing on their bill In that scenario, and very likely that only those with usage patterns benefiting the network would change their pricing structure. Those who are driving the negative impact on the network (and the capital expenditure policy makers were concerned about), would remain on their original pricing structure as it would not affect them financially for the impact they are having on the grid.

It has also been said that the role of retailers is to manage risk in the National Electricity Market (NEM), and network pricing risk is no different from the wholesale price risk they currently manage. This fails to understand the role retailers play as risk managers, and the nature of the risk itself. A retailer has an array of tools available to manage wholesale price risk. Predominantly, retailers procure financial derivatives, are often vertically integrated with generation, and will utilise demand response to manage the risks from the highly volatile NEM spot market. There are no comparable tools available for network pricing risk. Whilst it could be argued that economies of scale will enable retailers to balance the impacts of network pricing, this is only true for those retailers large enough to have a representative customer base. For smaller retailers, this will be impossible.

A better solution here would be for retailers and networks to work together to develop an actionable network tariff or suite of tariffs that retailers can translate into a customer product/s that customers too can understand. This was achieved in Victoria to some extent with the most recent approved draft TSS reflecting to date an outworking of genuine consultation. Network objectives were able to be met without overly complicating pricing structures.

Some have suggested that if network pricing decisions were re-opened to revisit the TSS and network pricing structures, it would suggest that networks are a riskier investment than the framework envisaged, and that their rate of return should be increased to offset this additional regulatory risk. The AEC would strongly refute this position. There is no additional risk to a network business from delaying the transfer of customers from one tariff to another during a regulatory period. Networks operate under a revenue cap, meaning their total revenues are fixed for a five-year period. If they over-perform and network expenditure is lower, they are allowed to keep the additional revenues as an efficiency incentive. The only impact of delaying the transfer of customers to new pricing structures is that the network may be less efficiently utilised, which the AEMC states would be the case even under the proposed rule that requires EIC before a customer sees a new pricing structure.

The AEC strongly agrees with the concerns raised by consumer advocates that it is unreasonable for small customers to be exposed to highly complex tariffs such as demand tariffs. For the AEMC, an interim rule to preclude a customer from being assigned to one of these network tariffs without their consent is a good start, but it is a rule that should be placed on the party in complete control of the pricing structure, the network itself. Retailers would not be changing customer pricing structures without EIC if the network

[16] See, for example, Energy Consumers Australia (2024) Cost reflective prices aren't very cost reflective pp.5-6

tariff they were exposed to was not changing. In circumstances where a new network tariff would be beneficial, individual customers can opt into a more complex pricing structure with the support of their retailer. Where customers want other pricing options, competition will encourage these outcomes, as is the case today with many customers opting into pricing that varies throughout the day, or even highly complex pricing that follows the wholesale price of electricity.

But such a rule should only be interim. The broader review of electricity pricing for a future energy system is a critical piece of work that should be prioritised by governments, regulators, industry, and consumers. The AEC is pleased that the AEMC is taking this review seriously, and in particular, welcome their decision to consult on a Draft Terms of Reference. This review must be set up in such a way to ensure the right questions are considered that will deliver an outcome that enables more efficient utilisation of the network and lower prices. It must also foster a positive relationship between retailers and their customers, as they work together to benefit from an energy system rapidly transitioning, to one where consumers have opportunities to participate if they are willing and able, and treated fairly where they are not.

We look forward to working with the AEMC, the AER, networks, and consumers to deliver on this opportunity over the longer term. In the meantime, a short pause on network tariff reassignments seems a prudent step to prioritise consumer price stability, without the unintended consequences that will come from the AEMC's proposed rule.

The AEC has written this submission with a focus on the optimum consumer safeguards to accompany the acceleration of smart meter deployment. In addition, the AEC draws the Commission's attention to submissions from AEMC members which emphasise the serious concerns with proposed implementation timeframes.

Any questions about this submission should be addressed by email to jo.desilva@energycouncil.com.au or by telephone on 03 9205 3100.

Yours sincerely,

Jo De Silva

Jo De Silva
General Manager Retail Policy