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Stephanie Jolly
General Manager, Market Performance
Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601

By email: DMO@aer.gov.au

Dear Ms Jolly,

RE: Consultation on Default Market Offer Prices: Options Paper on the methodology to be adopted for the 2022-23 Determination (and subsequent years)

The South Australian Council of Social Service (SACOSS) is the peak body for non-government health and community services in South Australia with a mission to advocate for the interests of vulnerable and disadvantaged people across the state. We thank the Australian Energy Regulator (the AER) for the opportunity to comment on its *Options Paper on the methodology to be adopted for the 2022-23 Default Market Offer Prices Determination (and subsequent years)* (the Options Paper).

This Options Paper represents the first step in the AER's process to determine Default Market Offer (DMO) prices for 2022–23. The DMO is the maximum price an electricity retailer can charge a customer on a standing offer, as determined by the AER each year. This will be the AER's fourth DMO determination (DMO 4). For DMO 4, the AER has committed to a holistic review of its overarching approach to setting the DMO, including an examination of the assumptions that underpin the methodology, in order to ensure the DMO achieves its policy objective of protecting standing offer customers from unjustifiably high prices.

The DMO price determination applies to small business and residential customers in South Australia (SA), New South Wales (NSW) and south-east Queensland (where there is no other retail price regulation).

As noted in the Options Paper, the AER must determine DMO prices for 'small customers' of certain types (each category includes customers with solar tariffs). These types are:[1]

[1] AER, Options Paper on the methodology to be adopted for the 2022-23 Default Market Offer Prices Determination (and subsequent years), 25 October 2021, p.

• *Residential customers* – on flat rate or TOU tariffs who use electricity mainly for personal, household or domestic use, and whose prices do not include a controlled load tariff.
• *Residential customers with controlled load* – on flat rate or TOU tariffs who use electricity mainly for personal, household or domestic use, and whose prices include a controlled load tariff.
• *Small business customers* – on flat rate tariffs with no controlled load, and who use less than 100 megawatt hours (MWh) per year.

The AER is not currently required to determine an annual price and usage for customers on other tariff types, such as:
• tariffs with a demand charge
• small business controlled load and TOU tariffs
• tariffs offered in embedded networks.

In performing its functions, the AER has identified one of its core objectives is to protect vulnerable consumers, while enabling consumers to participate in energy markets. SACOSS considers the AER's overarching goal should be to ensure the standing offer / DMO meaningfully operates as a default protection for *all* consumers who are not engaged in the market, chose not to engage, or cannot engage in the market. This is particularly important for customers in vulnerable circumstances, as identified in the ACCC's Retail Electricity Pricing Inquiry Report:[2]

> *'Consumers facing particular hardship and socioeconomic barriers to effective engagement in the electricity market are unlikely to get all of the benefits that competition can offer in this market.'*

The essential nature of electricity, and its potential to impact on the health, wellbeing and financial sustainability of households means it is vital consumers are able to access a fair and efficient price for this essential service. SACOSS agrees with and supports the principles contained in PIAC's submission to the AER on this consultation, including that to protect consumers and to promote their interests, the **DMO must be an efficient and fair price all consumers can default to when no other choice is made, or can be made** (as is the case for prepayment and embedded network customers).

Against the background of the fundamental principles underpinning the purpose and intent of the DMO, this submission is largely concerned with the need for the AER to ensure the following issues are properly **investigated and addressed** in determining the DMO 4 methodology for residential customers in SA:

- the impact of the mandatory Time of Use (TOU) standing offer / DMO tariffs on customers in South Australia, and guarantees that the TOU DMO will not further disadvantage already vulnerable customers in SA, and
- the need for the DMO in South Australia to reflect the ongoing reduction of wholesale electricity prices in our State.

[2] ACCC, Retail Electricity Pricing Inquiry Report, June 2018, xii

Local requirement for mandatory Time of Use (ToU) standing offers for smart meter customers in SA (both residential and small business)

One of the changes made under the South Australian Government's 'Smarter Homes' Regulations[3] (which came into effect on 28 September 2020), was intended to reform the retail tariff structure **of the standing offer** in SA, to reflect the TOU network tariffs approved by the AER in SA Power Networks' Tariff Structure Statement (TSS).

Pursuant to section 22(1a) of the *National Energy Retail Law 2011* (NERL) and Regulation 6A *National Energy Retail Law (Local Provisions) Regulations*, retailers in SA are now **required to have a standing offer for smart meter customers** that includes:

- SAPN's TOU tariff structure **OR**
- SAPN's Demand tariff structure for residential prosumer OR
- A tariff structure determined by the retailer (which could be flat tariff), **IF** the retailer has a TOU market offer that is approved by the Minister.

SACOSS has not been advised of any 'generally available market offers' that have been approved by the Minister.

By way of background, SACOSS considers it is worth setting out the relevant section of the NERL and Reg 6A of the Local Regulations in full, below. Part 2 of the NERL deals with the '*Relationship between retailers and small customers*'. Division 3 in Part 2 deals with '*Standing offers and retail contracts for small customers*', and Section 22 in Division 3 deals with '*Obligation to make offer to small customers*' which provides:

> ***22—Obligation to make offer to small customers***
> *(1) A retailer must make an offer (a standing offer) to provide customer retail services to small customers for whom it is the designated retailer—*
> *Note—*
> *This subsection is a civil penalty provision.*
> *(1a) If—*
>
> > *(a) a small customer has an interval meter; and*
> > *(b) a local instrument of this jurisdiction declares that this subsection applies in relation to this jurisdiction,* ***then a retailer's standing offer must include****—*
> > *(c)* ***such tariff structures as may be prescribed by local instrument****; or*
> > *(d) if and to the extent that a local instrument declares such Rules to apply—such tariff structures as may be prescribed by the National Energy Retail Rules in connection with the operation of this subsection.*
>
> *(1b) In connection with the operation of subsection (1a), a local instrument applying under subsection (1a)(c) or the Rules applying under subsection (1a)(d) may include provisions that will allow a small customer to elect that a certain specified tariff will, or will not, apply in relation to the customer.*

[3] See:https://www.energymining.sa.gov.au/energy_and_technical_regulation/energy_supply/regulatory_changes_for_smarter_homes

Regulation 6A of South Australia's *National Energy Retail Law (Local Provisions) Regulations* (Local Regulations) declares that subsection 22(1a) applies in relation to South Australia and prescribes tariff structures for the purpose of subsection 22(1a)(c) of the NERL:

> ***6A—Tariff structures***
> *(1) Section 22(1a) of the National Energy Retail Law (South Australia) applies in relation to South Australia.*
> *(2) The following tariff structures* ***are prescribed*** *for the purposes of section 22(1a)(c) of the National Energy Retail Law (South Australia):*
> > *(a) in the case of a residential customer—*
> > > *(i) the time of use tariff structure applying under the residential time of use tariff published by SA Power Networks; and*
> > > *(ii) the demand tariff structure applying under the residential prosumer tariff published by SA Power Networks;*
> >
> > *(b) in the case of a business customer who consumes energy at business premises below the upper consumption threshold—*
> > > *(i) the small business time of use tariff structure published by SA Power Networks; and*
> > > *(ii) the small business time of use with demand tariff structure published by SA Power Networks;*
> >
> > *(c) in the case of an eligible retailer—a tariff structure determined by the retailer.*
>
> *(3)* ***A retailer's standing offer need only include 1 of the tariff structures prescribed by subregulation (2)(a)*** *and 1 of the tariff structures prescribed by subregulation (2)(b), as determined by the retailer.*
> *(4) In this regulation—*
> ***eligible retailer*** *means a retailer that the Minister is satisfied—*
> > *(a) has a generally available market offer that provides efficient signals to customers about when to use energy; and*
> > *(b) is using its best endeavours to market that generally available market offer to customers.*

SA Power Networks' Pricing Proposal for 2021-22, approved by the AER, has identified one of the key changes from the 2020-21 Pricing Proposal is the delay of the mandatory reassignment of smart meter customers (both residential and small business) to TOU Tariffs from 1 July 2021 to the end of December 2021:[4]

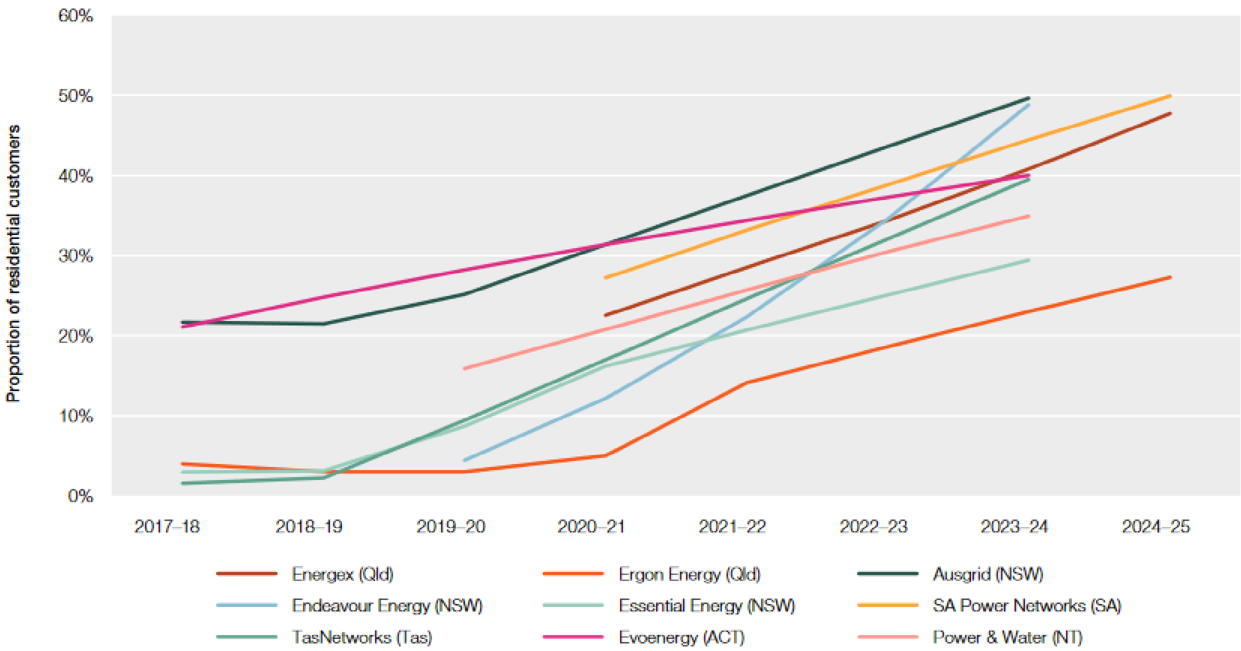
> '*This section outlines the key changes for 2021/22 compared to 2020/21 for Residential customers:*
> • *Mandatory reassignment of Residential Time of Use (ToU) tariffs for Type 4 meter customers will be delayed up to 6 months with reassignment complete by 1 January 2022.*
> • *Residential ToU Plus trial tariff is available to opt-in from 1 July 2021 with a maximum of 8,000 customers eligible to participate.*'

[4] SA Power Networks Annual Pricing Proposal 2021-22, ,p.9

Importantly therefore, smart meter customers **cannot choose flat rate tariff offers** after December 2021 in SA (currently around 20% of customers), unless the retailer has a market offer approved by the Minister and decides to continue to offer flat rate tariffs.

The AER's State of the Energy Market Report 2021 [5]shows that by 2024-25 around 50% of SA customers will be assigned cost-reflective tariffs:

Figure 3.9 Projected assignment of cost-reflective tariffs for residential consumers – electricity distribution networks



Source: AER analysis of unpublished forecasts supplied by regulated electricity distribution businesses.

Eventually, all customers in SA will be smart meter customers, and therefore all standing offer customers will be on a TOU standing offer, in line with Reg 6A (unless the retailer has a DMO / TOU offer approved by the Minister). This raises some concerns around how the ToU DMO is calculated over the next few years, and whether there is enough data to show usage patterns of those customers. Importantly, the methodology for DMO 4 will need to consider the mandatory TOU standing offers for SA smart meter customers, the lack of available TOU market offers for those customers, the inability to switch to a flat rate tariff and the increasing number of smart meter customers in SA over the coming 5 years.

It is widely accepted that standing offer customers are largely disengaged customers (which was one of the reasons the DMO was introduced), and it follows that those customers may be less likely to be able to move their usage patterns to avoid the **peak tariffs in South Australia between 6am -10am and 3pm to 1am (14 hours per day),** and in fact may not even be aware of the changes in pricing structures and the need to move usage. This could

[5] AER, State of the Energy Market Report 2021, p.142

lead to much higher bills for those customers, who are already likely to be in vulnerable circumstances.

It's also worth noting that small business customers with a smart meter on a standing offer are also being moved to TOU offers in line with Local Reg 6A, but the AER does not apply a TOU DMO to those small business customers – we are unsure how this will work for small businesses that may face higher tariffs during TOU peak periods when they can't shift their energy usage (like restaurants at breakfast and dinner times). We understand 15.5% of small business customers in SA are on standing offers, we don't know how many of those small businesses have smart meters.

If all SA smart meter customers are being automatically reassigned to TOU standing offer contracts in line with Reg 6A, it follows that the retailer cannot charge more than the TOU DMO. Will smart meter customers in SA be able to access a flat rate tariff if a TOU tariff does not work for their household? The whole DMO is predicated on the basis of customer choice,[6] and it is imperative the AER consider the absence of choice when determining the DMO in SA. There are real concerns if these customers don't have access to market choice, and are left with an expensive TOU standing offer (capped at an **inefficient DMO**). The importance of the TOU DMO being used as a reference price should also be of primary concern, given the broader impacts on pricing structures for all offers.

Requirement for monitoring and reporting of TOU data

As part of its price setting functions, the AER is required to determine:

- how much electricity a broadly representative small customer of a particular type in a particular distribution region would consume in a year and the pattern of that consumption (the model annual usage)
- a reasonable total annual price for supplying electricity (in accordance with the model annual usage) to small customers of a type in a region (the DMO price).

The AER is not required to determine the pattern of consumption in the case of small business customers, which may be problematic for small businesses on standing offers in SA, in circumstances where businesses with a smart meter are automatically moved onto a TOU standing offer.

As outlined above, SACOSS' main concern is to ensure customers are not disadvantaged by mandatory TOU offers, and continue to have choice (which is an underlying presumption in setting the DMO). We are seeking the distributional impacts of the mandatory TOU standing offers are **thoroughly monitored and reported on** by the AER in South Australia, as we are not confident that the SA government will be undertaking this task.

As outlined in the Table 2.1 in the Options Paper, there are currently 67,064 residential standing offer customers in SA (8.4% of residential customers), and 13,634 small business customers on a standing offer (or 15.5% of small business customers). We don't know how

[6]The substantial difference between the DMO price and the lowest offer in each region would provide incentives for DMO customers to shop around,

many of these customers use a smart meter. We do know that AGL moved 17,000 of its residential DMO smart meter customers onto a TOU offer on 1 July 2021.

We **strongly urge** the AER (or the ACCC using its investigative powers) to obtain data from AGL relating to the peak, off-peak and solar sponge standing offer rates, as well as usage patterns and energy costs of these 17,000 customers for (*at least*) the six-month period from 1 July 2021 to 1 January 2021, comparing this data to the six-month period *prior to* the introduction of TOU standing offers (1 January 2021 – 30 June 2021). Whilst 12 months of TOU data would be best (to accommodate changes in weather and associated seasonal usage patterns), at least the AER would have some idea of how the usage of **largely disengaged customers** automatically shifted to a TOU tariff changes (if at all), and whether costs increase compared with pre-TOU rates. Currently, there is very little data to gauge the impact of TOU offers on usage patterns or costs for these customers who are potentially in vulnerable circumstances, and may have no knowledge of the change in charging structure. We would like to see this data published in future consultation papers on the DMO, prior to the AER making its final determination.

Importantly, the AER must take into consideration the need for retailers to provide lower peak prices for TOU offers, to more accurately reflect the wholesale prices in South Australia (as noted below). Currently, retailers are offering a lower shoulder (or solar sponge tariff), but making up the difference in peak pricing, when there is absolutely no rationale for them to have this peak pricing in SA based on the retailer's costs. It will be incredibly difficult for consumers to avoid a 14-hour peak period with an unjustifiably high 39c per c/kWh[7] tariff. This is particularly concerning given households are automatically being shifted onto these offers with no choice, potentially leading to quite severe impacts on vulnerable groups, particularly for those with less ability to shift load. As noted above, the AER needs to track usage statistics for the rate types separately, otherwise there will be insufficient information to evaluate impacts of different rate design decisions.

Relevantly, and in line with the AER's objective to protect vulnerable consumers, it is worth noting a study from the United States which found that '*assignment to TOU rather than control disproportionately increases bills for households with elderly and disabled occupants, and predicts worse health outcomes for households with disabled and ethnic minority occupants than those for non-vulnerable counterparts. These results suggest that vulnerable groups should be considered separately in DSR rate design, and future pilots should seek to determine which designs most effectively avoid exacerbating existing energy injustices or creating new ones'*.[8]

[7] We understand this is AGL's TOU peak rate 6am – 10am, 3pm-1am.

Time Of Use				
Peak	6am - 10am and 3pm - 1am every day	c/kWh	35.75	39.325
Off-Peak	1am - 6am every day	c/kWh	22.80	25.080
Shoulder	10am - 3pm every day	c/kWh	19.49	21.439
Supply Charge		c/day	89.85	98.835
(Reference Price comparison below)				

[8] White, L.V., Sintov, N.D. Health and financial impacts of demand-side response measures differ across sociodemographic groups. *Nat Energy* **5,** 50–60 (2020). https://doi.org/10.1038/s41560-019-0507-y

To address the equity concerns surrounding TOU rates, a Policy Brief[9] by the authors of the study recommended that:

- *Policies are needed to ensure that demand-side response does not increase hardships for vulnerable groups.*
- *Different vulnerable groups will have different capacities to respond to rates using price signals, so demand-side measures should be carefully targeted rather than 'one size fits all'.*
- *Potential time-of-use rates should be tested using scientifically rigorous methods before widespread implementation, with separate evaluation of impacts on different groups.*
- *People who are elderly, have disabilities and/or are members of minority groups will likely require particular attention in future pilots and policies.*

In setting the methodology for determining the TOU DMO, SACOSS is seeking the AER gather relevant data and carefully consider the impacts of TOU offers on disengaged customers. In relation to stakeholder Q.20, we consider the AER should use a separate weighting for each network area.

Q.15 Should our existing assumed hedging strategy be adjusted to allow for a higher level of spot market exposure? And if so, what is the appropriate level of exposure? (please also consider this question in conjunction with Margin for forecast error discussion below).

The DMO in SA should reflect the ongoing reduction of wholesale electricity prices in SA. Although there are risks for retailers with continued price volatility, and other associated costs such as the frequency control and ancillary services (FCAS) market, SACOSS considers that customers in SA are not benefiting from lower wholesale pricing. Option 1, of the risk averse strategy of setting the DMO pricing of having a long 24 – 36 month hedge book in SA is not appropriate where wholesale prices continue to fall and go into negative in SA. SACOSS feels that a less risk averse strategy for retailers (Option 2) is more appropriate to the current and projected conditions of lower wholesale pricing in SA. It is imperative that consumers in SA begin to see lower retail electricity costs that reflect the amount of renewable energy in the state, which is lowering wholesale electricity prices.

Energy affordability in SA and the importance of setting a fair and efficient DMO

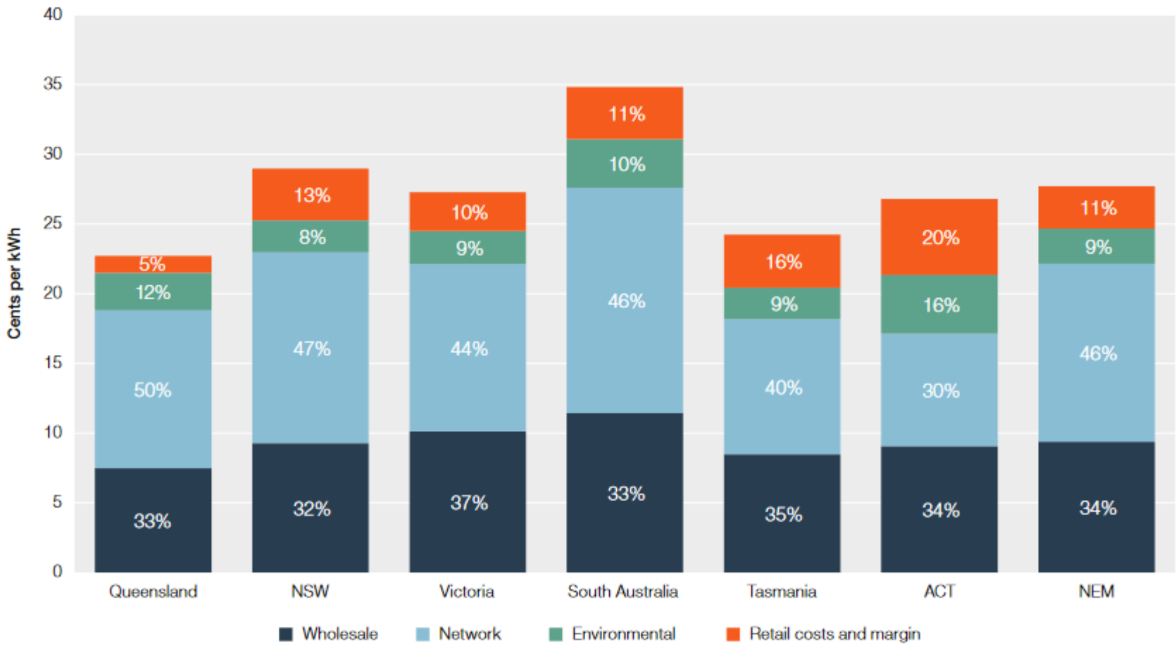
Speaking broadly, SACOSS considers it is important to emphasise that energy affordability continues to be the primary concern for South Australian energy consumers, particularly low-income consumers. The AER's recent *State of the Energy Market Report*[10] shows that while South Australia has the second lowest electricity use in the NEM, electricity prices were 16–49% higher than other NEM regions. Importantly, low-income households in SA

[9]White, L.V., Sintov, N.D. Policy Brief, 16 December 2019, Varied health and financial impacts of time of-use energy rates across sociodemographic groups raise equity concerns https://www.nature.com/articles/s41560-019-0515-y

[10] AER, State of the Energy Market 2021, June 2021, p. 275

spent around 5.5% of household income on energy bills, this is the highest electricity bill to income ratio in low income households in the NEM, after Tasmania (see Figure 6.13, below).[11] Network costs currently represent 46% of a residential electricity bill in SA, a significant proportion of the highest average energy bill in the NEM (see Figure 6.8, below).

Figure 6.8 Composition of a residential electricity bill

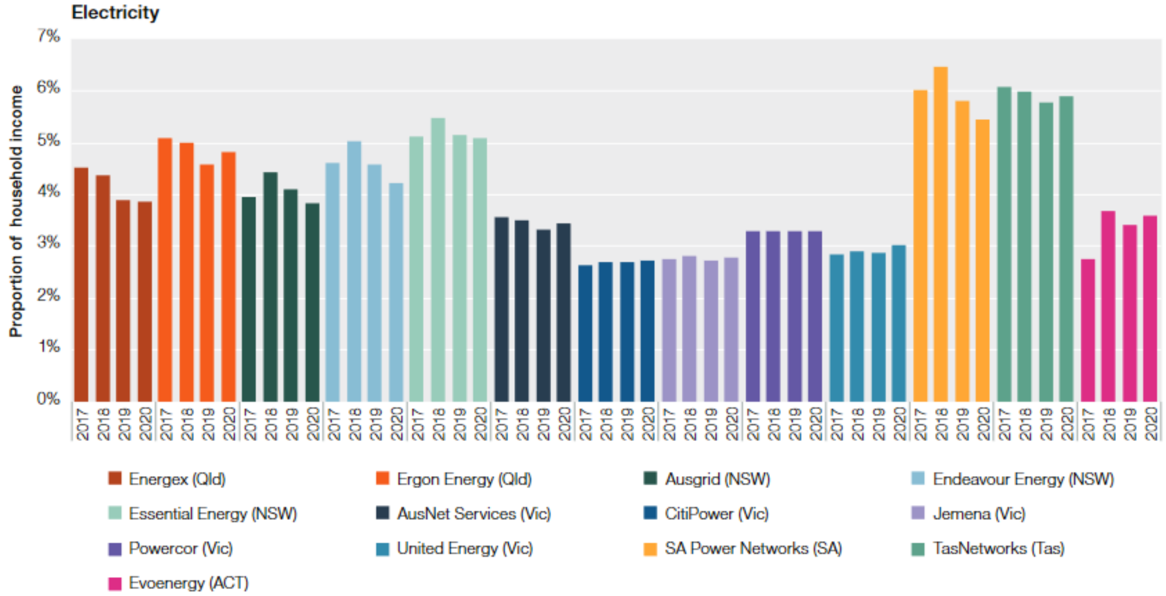


kWh: kilowatt hour.

Note: Data are estimates for 2020–21. Average residential customer prices excluding GST. Percentages may not add to 100% due to rounding.

Source: AEMC, *Residential electricity price trends 2020*, Final report, December 2020.

Figure 6.13 Energy bill burden on low income households



[11] AER, State of the Energy Market 2021, June 2021, p. 274

This affordability context highlights the importance of setting a fair and efficient DMO, not just for standing offer customers, but for *all* customers where the DMO is used as a reference price. We are urging the AER to go back to first principles and acknowledge energy as an essential service, with the DMO reflecting the fundamental right of all customers to be able to access energy on fair and just terms, including prepayment and embedded network customers.

If you have any questions in relation to this submission, please contact Georgina Morris at georgina@sacoss.org.au or 8305 4214.

Yours sincerely,

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South Australian Council of Social Service