

20 March 2019

The Hon Dan van Holst Pellekaan MP
Minister for Energy and Mining
Member of the Executive Council
PO Box 974
ADELAIDE SA 5001

By email: dem.ministervhp@sa.gov.au

Dear Minister,

Network tariff reform is essential to deliver lower prices to electricity customers and to protect the less well-off

Thank you for joining us at the recent Board meeting of South Australia Power Networks (SAPN) on 5 March 2019. The engagement and openness that we have received from yourself and your office in addressing the tough energy challenges that the market is going through as it transitions to an energy mix reliant on widely distributed renewable energy and storage is refreshing. For better or worse, South Australia is currently most exposed to these changes and hence must lead the charge on the reform required.

Our discussion has prompted me to share with you some further thoughts on the importance of network tariff reform in delivering lower electricity prices to customers and to ensure equality and fairness. As the less well-off customers are the most exposed from this transition, if change is not made now, they may be left in a long-term unsustainable position.

To be clear, the primary issue I see is in relation to the network component of a customer's electricity bill which makes up approximately 30% of a standard residential bill. As electricity customers change the way they use and rely on the networks (i.e. the electricity grid) to satisfy their own needs, the charging model for these network tariffs must also change. It is important to note that the network companies do not benefit financially from any network tariff reform as they operate under a "revenue cap", which sees them only entitled to recover their allowed revenues irrespective of volumes. The issue is about ensuring that those who use the networks pay their fair share.

I accept that progressing tariff reform is a difficult political issue, with "winners" and "losers". However, the rationale for tariff reform itself is supported by COAG Energy Council, our energy institutions and regulators, network businesses, generators, retailers and proponents of new technologies such as renewable energy, solar panels, and batteries. The benefits are clear:

- Efficient price signals to end-users leads to more efficient use of energy and the energy supply system reducing the need for future investment in networks; and
- Efficient price signals to investors leads to more efficient investment in new generation and transfer capability at the right time and in the right place.

Tariff reform will result in some customers being worse off financially, but this is a relative assessment. Those customers that may be worse off are those that currently pay less than their fair share of the network as a result of the way they use energy and force a greater proportion of network costs to be recovered from other customers, particularly those customers who remain solely reliant on the grid. In a lot of cases the customers who remain solely reliant on the grid, and hence face increased network costs, are the most vulnerable and low-income energy customers.

Customers who can afford to invest in 'behind the meter' investments, such as solar panels and batteries, are reducing their contribution to paying for the network without reducing the costs they impose on the system – noting that approximately 90% of network related costs are fixed and the network is engineered around meeting peak demand requirements, which are not declining despite the introduction of these new technologies.

At its simplest, the absence of appropriate network tariff reform will result in those customers least able to afford it, paying more. Therefore, the absence of tariff reform will result in:

1. Continued increases in prices (through an increased allocation of costs, notwithstanding that total network costs may be declining) to customers who cannot afford solar panels and batteries as they end up paying a greater proportion of the cost of the electricity network.
2. Continued increases in prices to all customers where peak demand continues to grow as the sun goes down.
3. Continued increases in prices from the need for network augmentation when new generators connect to the network at locations that exacerbate constraints in the network.
4. Continued increase in prices from congestion in the electricity networks impacting on wholesale energy prices.


We recommend:

- **Cost Reflective Network Tariffs** – Support network companies to adopt cost reflective network tariffs that are passed through to customers. Most Networks already have demand-based tariffs for larger customers, and more efficiently structured tariffs such as time of use tariffs should be rolled out to residential customers through their retailer.
- **Transparency of Network Tariffs on Customer Bills** – Require retailers to clearly identify the network component of the charge (and any changes) on a customer's bill. This will enable customers to better understand the impact of changing patterns of use and the value of new 'behind the meter' technologies on their overall bill.
- **Support Packages for Vulnerable Customers** – Develop targeted support packages for low income and vulnerable customers that are unable to change their electricity use and would be worse off if retailers passed through the cost reflective network tariffs. The cost of this targeted support is likely to be much less than the increased cost to all customers of future inefficient network and generation investment.
- **General Electricity Pricing Reform** – Policy setters should also consider broader pricing reform, for the non-network related component of an electricity customer's bill to ensure efficient use of the whole energy supply system and signal efficient investment in the system when and where it is needed. This could include time-of-use tariffs where appropriate.

There are challenges associated with network pricing reform. However, the size of the problem and the difficulty of addressing it will only grow with continued delays. More and more customers will invest in solar panels and batteries which will only compound the issue. South Australia is facing this challenge now, and the cost to government of supporting low income and vulnerable customers will only increase while the benefit of new technologies and lower network costs will be captured by a small minority.

Again Minister, thank you for the time last week. Please do not hesitate to contact me on (02) 9086 3600 if you'd like to follow-up on this issue, and I am also frequently in Adelaide if you'd like to meet in person.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Rick Francis".

Rick Francis
Managing Director

cc. Rob Stobbe, CEO SA Power Networks