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Tuesday, 23 October 2018

Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Dear Mr Pierce

RE: ERC0240 Global Settlement and Market Reconciliation, Draft Decision

ERM Power Retail Pty Ltd (ERM Power) welcomes the opportunity to respond to the AEMC Global Settlement and Market Reconciliation Draft Decision (the Draft Decision).

About ERM Power Retail

ERM Power is an Australian energy company operating electricity sales, generation and energy solutions businesses. The Company has grown to become the second largest electricity provider to commercial businesses and industrials in Australia by load¹. A growing range of energy solutions products and services are being delivered, including lighting and energy efficiency software and data analytics, to the Company's existing and new customer base. The Company operates 662 megawatts of low emission, gas-fired peaking power stations in Western Australia and Queensland.

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General Comments

Local retailers have long enjoyed the benefits of incumbency, including the retention of many customers that have failed to engage the competitive market, and many of whom, at least outside of Victoria, remain with accumulation meters. The Draft Decision proposes a move away from settlement by differencing to global settlements, whereby all retailers would be billed for the loss adjusted metered energy consumed by their customers within a distribution area. 'Unaccounted for Energy' (UFE) would be socialized to all customers in distribution area, pro-rated based on their 'accounted for energy'. This allocation is irrespective of whether or not the customer actually contributes to the incidence of UFE.

The Commission has argued that a move to global settlements will produce a net benefit to customers by:

1. Improving transparency, leading to fewer settlement disputes and lower levels of UFE,
2. ensuring competition on equal terms, and

¹ Based on ERM Power analysis of latest published financial information.



3. enhancing incentives to reduce UFE by improving risk allocation.

ERM Power considers that the Commission's cost estimate for the implementation of global settlements is grossly underestimated. The Commission has suggested that one-off implementation costs to the industry would be less than \$10 million, incremental to the changes for 5 Minute Settlement, and that there would be only modest costs to retailers². We believe the Commission has overlooked the material costs to retailers from this proposed rule change, including transformations to retailers' settlement calculation systems, forecasting, reconciliation processes, customer contract terms and conditions, billing systems to accommodate the dynamic charge, IT project costs, staffing for change management and the impact on prudential security (which will be ongoing).

Whilst ERM Power acknowledges that transparency will be improved under global settlements, we question the claims around a net benefit from enhanced incentives by levying UFE on **all** customers and strongly believe that our large commercial and industrial customers will not benefit from these changes but will be financially worse off.

Under a global settlement regime, small accumulation metered customers are more likely to be the source of UFE and incentives to reduce UFE are more likely to be realized if the prices to these customers reflect the costs of losses they generate. Importantly, UFE is more likely to reduce if it is solely allocated to accumulation, type 7 and unmetered customers as these customers will be incentivized to install more accurate advanced metering. If global settlement is to be implemented, UFE should only be allocated to accumulation, type 7 and unmetered customers to avoid large and interval metered customers unfairly cross subsidizing the customer loads responsible for UFE.

The greatest incentive to reducing UFE and achieving dynamic efficiency is through a move to advanced metering

In the Draft Decision, the Commission acknowledges that a "benefit of advanced meters is that settlement data becomes more accurate as the advanced meter fleet grows and the accumulation meter fleet retires"³. Beyond missing connection points, theft and meter fault issues that are inherently a small customer load anomaly, a significant proportion of UFE is likely to be generated through AEMO's profiling estimation of accumulation data for settlement. Advanced metering dispenses with the requirements of profiling data and ensures settlement reflects actual meter data, measured for each interval. The Commission recognizes in the Draft Decisions that, in an effort to reduce UFE, encouraging all retailers to replace type 6 accumulation meters with interval meters will seek to reduce profiling errors and provide additional benefits of revenue protection measures that are inherent in advance metering.⁴

However, the Commission has suggested that a reallocation of the costs of UFE from the incumbent retailer to all retailers will incentivize retailers to address the causes of UFE and more likely lead to a reduction in UFE. It has argued this position with citing the reduction in UFE that occurred in New Zealand from the introduction of global settlement in 2008⁵. ERM Power suspects that the reduction in UFE in New Zealand was more likely to be the result of increasing advanced meter penetration as opposed to the reallocation of losses from the incumbent retailer. This was observed by the New Zealand's Electricity Authority's recent decision on the '*Guidelines on the calculation and use of loss factors for reconciliation purposes*', in which the Authority noted that although UFE has reduced for a variety of reasons,

² AEMC, Global Settlement and Market Reconciliation, Draft Rule Determination, 30 August 2018, page iii

³ Ibid page 12

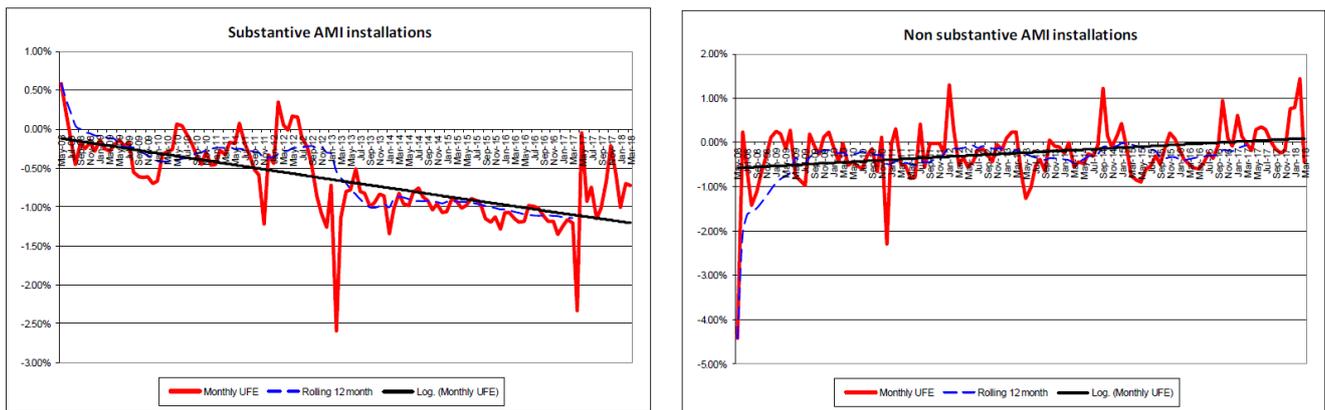
⁴ Ibid page 28

⁵ Ibid, page ii.



“the reduction in UFE is most marked on networks where the majority of metering installations have been upgraded to advanced metering infrastructure (AMI). Those networks that have not had substantial AMI upgrades have not had as much reduction in UFE and, in few cases UFE has increased.”⁶

These findings of UFE in New Zealand were illustrated in the two graphs below.



Source: NZ Electricity Authority, Decision – Guidelines on the calculation and the use of loss factors for reconciliation purposes, 26th June 2018.

It appears the greater the concentration of advanced metering, the more likely UFE will trend downwards. Conceptually the greatest incentive to reduce UFE comes from implementing advanced metering and improving meter accuracy.

Large Customers will be unfairly levied with UFE costs but do not contribute to the drivers of UFE

The Commission rightly acknowledges that “to promote efficient outcomes in the electricity market, retail charges should accurately reflect the quantity of electricity consumed and prices should not include inefficient cross subsidies”.⁷ Based on the Commission’s own assessment principles, risks should be allocated to the parties who have incentives and ability to efficiently manage them. Therefore, UFE should not be levied on parties that do not contribute to UFE. ERM Power is concerned the proposal to levy UFE on all customers in the distribution area will actually lead to a cross subsidy whereby large customers, by their consumption will be levied with the greatest proportion of UFE but are unlikely to create it. Moreover, retailers of large customers will not be able to control the risks surrounding UFE.

The Draft Decision identifies that UFE includes losses from inaccurate metering equipment, theft, unaccounted metering connections, and accumulation metering profiling inaccuracies. These sources of losses are attributable to accumulation metering and predominantly small customers. Large customers have advanced interval metering, which is most accurate and routinely tested in accordance with the National Electricity Rules. Arguably commercial and industrial customers are too large for undetected metering connections or theft.

If the Draft Rules are implemented, UFE for our large customers will be an unavoidable component of their consumption and although these customers have invested in accurate metering they will be penalized for the inaccurate metering of others.

⁶ New Zealand Electricity Authority Decision – Guidelines on the calculation and the use of loss factors for reconciliation purposes, 26th June 2018, page 6,

⁷ AEMC, Global Settlement and Market Reconciliation, Draft Rule Determination, 30 August 2018, page 21



Allocation of UFE to accumulation metered and unmetered loads

We suggest that the Commission should consider a methodology that apportions UFE to accumulated metered load, type 7 metered customers and unmetered load only. This would allocate the risks appropriately and incentivize a reduction in UFE through the move to advance metering. There will be a greater reduction in UFE through greater accuracy in estimation methodologies of unmetered load and type 7 metering, and an incentive to ensure greater accuracy in Net System Load Profiling. Ultimately, investment in advanced metering would reward customers for contributing to dynamic efficiencies through the reduction in the incidence of losses and therefore UFE.

Please contact me if you would like to discuss this submission further.

Yours sincerely,

[signed]

Libby Hawker

Senior Manager, Regulatory Affairs

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