



Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

**Wholesale Demand Response Mechanisms – Consultation Paper
(ERC0247)**

John
Dear Mr Pierce,

The South Australian Government thanks you for the opportunity to comment on the Wholesale Demand Response Mechanisms – Consultation Paper.

As stated in our rule change proposal, the South Australian Government considers creating a mechanism that transparently transfers the value of the wholesale demand response will create competition in the offering of demand response products and unlock demand response potential. We consider that the Rules should promote greater opportunities for consumers to participate in wholesale demand response. This will result in increased competition in the wholesale electricity market which may potentially contribute to a decrease in prices and improved reliability in the electricity market.

We wish to provide further clarity on the options for a transitional model, as raised in our initial proposal.

The value of wholesale demand response arises from the changed level of exposure to the wholesale price. The proposal seeks to allocate the value of wholesale demand response to a demand response provider (which may be shared by the consumer and the third party appointed by the consumer) through a regulatory mechanism. This has direct implications for market settlements.

We consider a co-optimised model, as briefly mentioned by the Commission in the Consultation Paper, would introduce the benefits of a demand response mechanism in as soon a period as possible. This separate demand response market would be operated by AEMO, and co-optimised with existing wholesale market.

Under this model a customer's retailer, the financially responsible market participant, would charge the customer based on their *actual* consumption, and the retailer would in turn purchase the actual load from the wholesale market. Both a continuation of the current arrangements with payments occurring in the same manner as is currently the case.

For this reason, there would be no need for a change to retailer systems under this approach, as the transaction would be an out of market, contractual arrangement between the customer and the retailer. Similarly, the transaction between the retailer and the wholesale market would occur using current AEMO systems.

A proposed new market participant, the demand response service provider (DRSP), would bid in to a separate wholesale demand response market. These bids would be for a quantity of wholesale demand response, the difference between actual and baseline consumption from its customers.

The DRSP would then be paid for dispatched demand response through this separate market. The price paid to the DRSP could be the same as the wholesale spot price or as a bid price. The DRSP could not, however, be dispatched at a price which was higher than the wholesale spot price as the two markets are co-optimised.

DRSPs could pay their customers a credit for their demand response. This would be an out of market, contractual arrangement between the individual customer and their DRSP.

The costs associated with paying DRSPs would be recovered from all customers in a smeared manner similar in principle to the cost recovery for the Reliability and Emergency Reserve Trader (RERT). The AEMC could also consider ancillary service cost recovery mechanisms. Given retailers already manage some market costs which are recovered in this type of manner, it is not expected that retailers would need to make significant changes to their systems.

Should the AEMC consider that there is a risk of significant additional costs from such a mechanism, there are mechanisms that could be put in place to manage such risks. For example:

- A cap could be placed on the level of demand response or cohort of market participants that can be settled in demand response market to limit the potential costs (noting that these should be outweighed by benefits to wholesale prices). This cap could be increased, or removed, over time as the market gains a better understanding of the costs associated with the demand response settled through a separate market.
- The transitional model could be limited to certain jurisdictions that have an immediate need for demand response, such as South Australia.

Retailers may also benefit under this approach through a reduced exposure to the wholesale market. Due to the customer's demand response, the retailer has avoided the costs of having to purchase some expected load from the wholesale market and are not exposed to the spot price for load that is shed.

While there would be no retailer systems changes required under this option, it has the benefit in reducing the overall cost. It also has timing benefits, as the transitional model could be in place in advance of any longer-term mechanism.

However, depending on the drafting of rules for this model, AEMO systems may need to be developed. The costs of establishing the separate market, and associated systems changes, would be recovered from all retailers. While these system changes would be required sooner, it is assumed these system changes would not be the same as those required for the longer-term wholesale DR mechanism.

Options that the AEMC could consider which may achieve the principles above, but limit costs associated with AEMO systems, could be:

- Allow demand response to be bid into the wholesale electricity market using the Market Customer category, with the market load classified as scheduled load. New rules could provide for cost recovery, price and other necessary limitations; or
- Develop rules for a limited transitional mechanism that would not prohibit AEMO using the NEM pre-production dispatch engine to manage the demand response market. In this circumstance, new rules would primarily need to deal with scope of the mechanism (i.e. MW / regions / number participants) and a cost recovery mechanism.

The South Australian Government has committed to reducing energy prices and ensuring a reliable grid. As we are committed to rewarding customers for managing their own demand, and therefore the introduction of a demand response mechanism in the wholesale electricity market, we would support the trialling of these transitional models in South Australia.

Should you have any questions in relation to this proposal, please contact Ms Rebecca Knights, Director - Energy Policy & Projects, Energy and Technical Regulation Division, on (08) 8429 3185.

Yours sincerely



Vince Duffy

Executive Director
Energy and Technical Regulation
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