



**EnergyAustralia**

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Dear Commissioners,

**Power of Choice Review: giving consumers options in the way they use electricity, draft report**

EnergyAustralia welcomes the opportunity to make a submission on the 'Power of choice – giving consumers options in the way they use electricity' draft report (*the draft report*).

EnergyAustralia is one of Australia's largest energy companies, providing gas and electricity to over 2.7 million household and business customers. We own and operate an integrated portfolio of energy generation and storage facilities across Australia.

We are committed to helping our customers with efficient solutions, and believe that consumers should be empowered to make energy choices that best meet their individual needs.

We agree with many of the propositions in the draft report, particularly the focus on facilitating more efficient pricing. However, we believe the proposed demand response mechanism for wholesale markets is unnecessary, overly complex and inefficient.

A detailed response to each of the recommendations in the draft report is attached. In particular we would like to highlight the following issues.

### *Flexible, cost reflective pricing is essential*

Flexible, cost reflective pricing is both necessary and sufficient to optimise demand side participation. As described in the draft report:

*‘An efficient demand response will occur when the costs to the consumer of supply (including both energy and network costs) is more than the costs of not consuming, i.e. the “opportunity cost” of not consuming. If a retail contract accurately reflects the cost of supply, including energy and network costs, consumers will change their consumption behaviour in response to market signals. In this situation consumers will decide whether the value of consumption is worth the cost incurred in the supply of electricity<sup>1</sup>.’*

The role of the National Electricity Law and Rules should be to establish a framework that allows efficient, cost reflective prices to flow through the supply chain. Consumers can then choose pricing plans that suit their needs.

We welcome the draft report’s recognition of the importance of efficient pricing in enabling optimal demand side participation.

### *Price deregulation and efficient network regulation*

Effective competition in retail and wholesale electricity markets, and efficient regulation of monopoly networks, are required to facilitate flexible and cost reflective pricing.

The regulatory and market structure needed to support efficient pricing in the NEM is already largely in place. However, policy leadership and regulatory reform is needed to remove barriers to efficient network and retail pricing:

- Retail electricity markets in the NEM are some of the most competitive in the world; however competition and efficient pricing for small customers is restricted by price regulation (outside Victoria). Deregulation of retail prices will facilitate efficient pricing to support Demand Side Participation (DSP). Community concerns should be addressed with accurate information and smooth transition arrangements.
- Transmission and distribution networks are subject to economic regulation as natural monopolies. Minor reform of the rules may be necessary to require development of more efficient and cost reflective network tariffs and incentives to support DSP.
- Wholesale markets in the NEM are highly competitive and deliver efficient, dynamic and cost reflective pricing. Large energy users can access cost reflective time varying prices through their retailer, and very large customers can purchase directly from the pool. No separate reform is needed to facilitate optimal DSP.

Competition is the most effective mechanism to facilitate efficient pricing. Retail price regulation undermines effective competition and restricts a retailer’s ability to innovate. The impact of price

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<sup>1</sup> Draft report pg 63

regulation on competition and innovation is most dramatic where jurisdictions set tariffs below the efficient long run cost of supply. While it may be superficially appealing in the short term to pay less than efficient costs, it is unsustainable and not in the long term interests of consumers.

Retail price regulation should be removed where a market is contestable and allows effective competition. We also agree with the AEMC's view that there is 'merit in removing or amending price regulation not only where competition is already effective, but also as a means of stimulating competition in retail markets<sup>2</sup>'. Where price regulation is retained, it is important that the framework promote competition, reflect long run costs and allow for flexible time based pricing options.

#### *Retail competition drives innovation and customer value*

Retail competition will drive the development of a range of products that allow consumers to choose pricing models that best suit their individual circumstances.

Distribution businesses should be required to develop efficient tariffs for network services, including time of use components and incentives for peak demand response where appropriate. Retailers are then best placed to combine energy and network components into a range of product choices to serve consumers needs (flexible, fixed, incentive based).

Flexible cost reflective pricing should be sufficient to enable efficient DSP by most consumers without the need to directly interact with their distributor, particularly when combined with appliances and devices capable of being programmed to operate at defined times and/or respond automatically to price signals. However, large and sophisticated industrial customers may still need to engage directly with distribution businesses on specific local network issues.

#### *Flexible cost reflective prices are equitable as well as efficient*

Traditional flat tariff regimes are inequitable and unfair, as well as inefficient. Customers with flat usage or low peak demand cross subsidise those with high peak demand. As demonstrated in research presented to the AEMC by the Brattle group, up to 80% of low income customers in the US may be over paying under flat tariffs. There is no reason to assume that a similar proportion of low income consumers would not benefit from the introduction of dynamic cost reflective tariffs in Australia.<sup>3</sup>

A diverse range of retail products will allow customers to save money by altering consumption patterns and/or choosing tariffs that best suit their consumption profiles.

#### *Appropriate transition is required*

Enabling efficient pricing requires the introduction of supportive technologies, reform of network tariffs and deregulation of retail prices.

A smooth transition path for small consumers is needed to facilitate community understanding and acceptance, and allow industry to develop and deploy appropriate products and technologies.

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<sup>2</sup> Draft report page 111

<sup>3</sup> Brattle Group 'Managing the benefits and costs of dynamic pricing in Australia'. 3 October 2012.

However, as noted in the draft report *'To encourage consumers to participate and realise the benefits of DSP, such arrangements should support consumer decision making and should not introduce, nor lead to, increased complexity. It is also important that sufficient consumer protection and other support mechanisms are in place.'*<sup>4</sup>

In this context we do not understand the rationale behind the draft report recommending complex new arrangements to allow multiple commercial entities to supply a customer through a single market meter, or to create a new mechanism for customers to access the wholesale pool price. In trying to 'gold plate' the market, such arrangements would increase complexity and cost, reduce or confuse customer protections, introduce inefficient distortions and are likely to delay transition to more efficient pricing.

Some consumers may benefit, but at the expense of other consumers who would bear the increased costs.

The electricity market should be designed to deliver economic efficiency in the interests of consumers. It should not be distorted to align with the business models of particular companies. If a company identifies a business model that can liberate additional value for customers, taking into account all the costs and risks, then they can obtain a retail licence and enter the market.

#### *Metering access and deployment*

We support the widespread adoption of metering technology necessary to support flexible pricing of energy and network services, and empower consumers, where it is economic to do so.

We believe that a contestable model is attractive in principle, and that the model proposed by the AEMC is worthy of further detailed examination.

However, we also recognise that the vast majority of mass market meters are currently owned and operated by distribution businesses and that advanced metering offers significant potential benefits for networks.

To support contestable metering, the following key components need to be addressed:

- Minimum Functional specifications that cater for both network and retail services;
- Separation of metering charges;
- Access arrangements and service standard that support benefits realisation; and
- Technology neutral platforms and protocols that encourage participation and innovation.

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<sup>4</sup> Draft report pg 32

### *Proposed wholesale market demand side response mechanism*

The draft report recommends the introduction of a new demand side response (DSR) mechanism to pay demand resources via the wholesale electricity market. We understand that the mechanism is targeted at large commercial and industrial (C&I) customers and essentially involves a three way transfer between the customer, retailer and AEMO:

- The DSR participant pays their retailer at their retail tariff against their baseline consumption;
- The retailer settles AEMO at the spot price for the customers baseline consumption; and
- AEMO settles the customer at the spot price times their reduction on baseline usage.

We do not support this draft recommendation as it is unnecessary and inefficient. We believe it would;

- Distort the efficiency of the contract market and investment signals;
- Be complex and costly to implement; and
- Impose costs on all energy consumers for the potential benefit of a few.

The wholesale spot market in the NEM already provides the efficient and dynamic real time prices necessary to optimise demand and supply responses.

The C&I sector of the retail market is highly competitive and there are no significant technical barriers or market failures that impede efficient pricing of energy for large commercial and industrial (C&I) customers.

The proposal appears to rest on the false assumption that it unlocks economic value that is not already accounted for. The DSR mechanism would essentially create a free option for the consumer to arbitrage between their negotiated retail tariff and the spot price. However, this value is already included in the negotiated retail tariff.

Price volatility is an intrinsic feature of the energy only gross pool market. Electricity retailers manage price and load volatility for consumers through the contract market. This is not a trivial or low cost risk management service and has significant value for customers and the market.

An effective contract market is vital to the efficient operation of the NEM and delivers benefits to all consumers. For example, in a study for esaa, ACILTasman estimated that a five per cent reduction in contracting across the NEM could lead to an increase in retail prices of up to ten per cent for households, and up to fifteen per cent for businesses.<sup>5</sup>

The proposed DSR mechanism increases risks for retailers and generators and would undermine the ability of the energy spot market settlement to fund an efficient contract market. This could be expected to reduce contract cover and/or increase hedging costs across the market.

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<sup>5</sup> [http://www.esaa.com.au/content/detail/national\\_electricity\\_market\\_modelling\\_ACILTasman](http://www.esaa.com.au/content/detail/national_electricity_market_modelling_ACILTasman)

## *Conclusion*

EnergyAustralia is committed to helping our customers with efficient energy solutions and we believe that consumers should be empowered to make energy choices that best meet their needs.

We agree with many of the propositions in the draft report, particularly the focus on facilitating more efficient pricing. We recognise the need for a smooth transition path to fully flexible pricing for mass market customers, however we do not support the proposed demand response mechanism for wholesale markets which we believe is unnecessary, overly complex and inefficient.

We thank the AEMC for the opportunity to respond to the draft report. For any questions regarding this submission, please contact me on (03) 86281034.

Yours sincerely

Signed for email

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## **Chapter 2 Facilitating consumer access to electricity consumption information**

### **Chapter 2 : Draft recommendations Part 1**

Chapter 7.7 (a) of the NER to clarify the requirements on a retailer when consumers request access to their energy and metering data. This would include provisions relating to the format and structure of data to be provided; the timeframes for delivery; and fees that can be charged.

Chapter 7 of the NER to require, at a minimum, a retailer to provide residential and small businesses consumers with information about their electricity consumption load profile. There may be a need to amend the National Energy Customer Framework (NECF) to ensure consistency of arrangements.

#### **AEMC Questions**

1. What should be the minimum standard form and structure of energy and metering data supplied to consumers (or their agents)? Should these arrangements differentiate between consumer sectors (ie industrial/ commercial and residential)
2. When do you think it is appropriate for a retailer (or responsible party) to charge a fee for supplying energy and metering data to consumers or their agents?

#### **EnergyAustralia response: Supported**

This is consistent with the existing requirement for retailers to provide information to customers under Section 28 of the NERR.

The minimum standard and format should be simple and practical for the customer to use. Data should be able to be provided and displayed via a web portal and other suitable electronic formats.

An option for a simple paper based reports should be retained for customers who are unable or unwilling to use electronic formats, however time of use data should only be required to be provided electronically.

There should be a limit on the number of 'free' requests that a consumer is entitled to make within any year, however we expect that many retailers are likely provide unlimited electronically data requests via the internet in the future.

### **Chapter 2 : Draft recommendations Part 2**

Chapter 7.7 (a) of the NER to enable agents, acting on behalf of consumers, to access consumers' energy and metering data directly from a retailer. This would include requirements on a retailer to provide consumers' energy and metering data to an authorised consumer's agent (third party), following explicit informed consent.

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consumers' energy and metering data to an authorised consumer's agent (third party), following explicit informed consent.

**EnergyAustralia response: Conditional Support**

Consumers hold the right to access, correct or scrutinise information that businesses hold about them, including information regarding usage.

We are not opposed to consumers engaging agents to act on their behalf, however in practise it is very difficult for retailers to ensure explicit informed consent has been obtained. Without evidence of consent and any conditions attached to it, retailers may inadvertently provide information beyond what the consumer has consented to. In practice it is generally simpler for the customer to request their data directly and provide it to their agent. The agent can easily assist the customer with this request.

It should be noted that only the FRMP is able to provide this service, as no other party can validate the duration of the customers connection with the NMI to prevent release of data belonging to a previous customer at the premise.

**Chapter 2 : Draft recommendations Part 3**

The NER to require AEMO to publish market information on representative consumer sector load profiles.

**AEMC Questions**

3. Do you agree that general market information should be published on consumer segment load profiles to inform the development of DSP products and services to consumers?

4. Is AEMO the appropriate body to publish such information, or should each DNSP be required to provide such information particularly where data will be at the feeder level where accumulation meters are installed?

**EnergyAustralia response: Neither support nor oppose.**

We are unable to determine what benefit the proposed recommendation would deliver. Publishing representative loads may not provide consumers with valuable information, and risks further confusion. With introduction of interval metering consumers will have access to their actual load profile. In the absence of interval metering consumers cannot receive or response to time of use pricing.

If the AEMC proceeds to require to publication of representative consumer sector load profiles, we agree that AEMO appears to be the body best placed to undertake this.



### **Chapter 3: Engaging with consumers to provide DSP products and services**

#### **Chapter 3 : Draft recommendations Part 1**

NECF is clarified to make it clear what arrangements apply to third parties providing “DSP energy services”. This should involve establishing criteria either in the NECF or the Australian Energy Regulator (AER) guidelines on retail exemptions. The criteria could include the circumstances where accreditation (or exemptions) of parties is required and the relevant provisions of the NECF that would apply (ie marketing rules, and the relevant enforcement and monitoring provisions).

#### **AEMC Questions**

5. What specific criteria could be used to determine whether elements of the NECF (ie marketing code) apply to third parties providing DSP energy services to consumers? That is, beyond Australian Consumer Law?

6. What requirements should be in place for these third parties? For example, what should be the form of authorisations/accreditations?

#### **EnergyAustralia response: Conditional Support**

We support review and clarifications of arrangements that apply to parties providing ‘DSP energy services’. There is considerable potential for consumer confusion and unintended impacts on consumer protections.

We believe that all parties providing energy services consumers within the energy market framework should be captured by the NECF or retailer authorisations. The same requirements and protections should apply to a company selling energy from the market to a consumer or selling energy response/ancillary services from the consumer to the market.

For example, a business selling:

- Electricity to a customer for any use (including charging an electric vehicle) should generally be an electricity retailer and subject to the same requirements as any other electricity retailers.
- Demand reduction from consumers to the market should be regulated in a similar manner to an electricity retailer.
- Products that may have demand response capability (such as electric vehicles) is not providing energy services within the energy market and should not require any authorisation.

We do not believe it is in the interests of customers to allow multiple commercial entities to supply a customer through a single market meter.

### **Chapter 3 : Draft recommendations Part 2**

The NER and NECF are clarified to outline the conditions when a distribution network business can engage directly with consumers to offer DSP network management services. This may involve establishing appropriate guidelines/process for the AER to apply and outlining which elements of the NECF apply.

#### **AEMC Questions**

7. Do you agree that existing rules and guidelines should be amended to clearly outline the circumstances when distribution businesses are able to directly contract with residential and small consumers to deliver DSP network management services/programs?

#### **EnergyAustralia response: Support**

We believe that review and clarification would be worthwhile.

Electricity retailers are best placed to develop products that allow customers to choose pricing models that best suit their individual circumstances. In general it not reasonable to expect most consumers to engage separately with distribution businesses and retailers to create their own products, combining network and energy components.

To simplify consumer interaction and drive customer focussed innovation through competition, it is important that the retailer owns the full relationship with the consumer - particularly for mass market customers.

The primary role of distribution businesses is to develop and publish a range of efficient tariffs for the monopoly network services, including time of use including incentives for peak demand reductions. Retailers are then best placed to combine energy and network components into a range of product choices to serve consumers needs (flexible, fixed, incentive based).

It may be reasonable to expect sophisticated large commercial and industrial customers to be in a position to engage directly with monopoly distribution businesses for additional demand reduction incentives, but not mass market customers.

With the introduction of flexible cost reflective pricing, and the availability of products able to set operating times and/or respond to these price signals, it is not evident that there is an enduring need for distribution to directly engaging with customers in respect to DSP.

Appropriate ring-fencing arrangements will be essential if regulated distribution businesses are able to provide DSP services in completion with retailers.

## **Chapter 4 Enabling technologies for DSP**

### **Chapter 4 : Draft recommendations Part 1**

A minimum functionality specification is included into the NER for all future new meters installed for residential and small businesses consumers. That specification should include, interval read capability and remote communications.

#### **AEMC Questions**

7. Should the minimum functionality specification for meters be limited to only those functions required to record interval consumption and have remote communication? Alternatively, should the minimum functionality include some, or all, of the additional functions specified in the SMI Minimum Functionality Specification?

#### **EnergyAustralia response: Conditional Support**

We support the establishment of a minimum specification.

We believe that a specification aligned with the SMI Minimum functionality specification is more likely to maximise net benefits and competition over time, while minimise the impact on customers associated with changing physical meters. In particular, the ability for retailers to be able to provide enhanced products for consumers through Home Area Networks (HAN) or software upgrades without requiring disconnection and physical replacement of the meter has obvious attractions for consumers and the market as a whole.

The determination of the minimum specification should seek to maximise expected economic benefits for consumers (network and energy), having regard for the costs. It does not appear that the AEMC has done the work to inform this decision.

### **Chapter 4 : Draft recommendations Part 2**

The installation of meters consistent with the proposed minimum functionality specification to be required in certain situations (e.g. refurbishment, new connections, replacements).

Such metering must also be installed on an accelerated basis for large residential and small business consumers (band 1) whose annual consumption is above the proposed defined threshold.

#### **EnergyAustralia response: Support**

We strongly support the widespread adoption of the metering technology needed to empower

consumers by facilitating flexible, efficient pricing of energy and network services where it is economic to do so. The incremental cost of installing a meter compliant with the established minimum specification when installing a new or replacement meter is likely to be relatively low.

However, the practical implications, costs and benefits of this recommendation are in part related to the nature and ownership of metering services and the minimum specification. These issues should be considered together.

#### **Chapter 4 : Draft recommendations Part 3**

Reforms to the current metering arrangements are necessary to promote investment in better metering technology and consumer choice. We have put forward a model where metering services are open to competition and can be provided to residential and small business consumers by any approved metering service provider.

If the new arrangements are implemented, then we advise that government consider removing the possibility of a mandated roll-out of smart meters

#### **AEMC Questions**

8. Does the separation of the provision of metering services from retail energy contracts remove the need for meter churn when a consumer changes retailer? Does this cause any unforeseen difficulties or create any material risk? Are there any alternative approaches to reducing the need for meter churn?

9. Are there sufficient potential metering services providers to facilitate a contestable roll out of AMI? Does the proposed model mitigate all the material risks of a contestable roll out? If not, should a monopoly roll out be adopted?

10. What should the exit fee when a consumer upgrades its meter from one provided by the local distribution business? Is the proposed fixed 30% of the cost of a replaced meter appropriate?

11. Does the option of a government mandating an AMI roll out within its jurisdiction act as a strong disincentive to a commercial roll out? Should the ability for these governments to mandate an AMI roll out be removed from the NEL?

#### **EnergyAustralia response: There is insufficient information and analysis to inform a decision on this recommendation.**

We strongly support the widespread adoption of the metering technology needed to empower consumers by facilitating flexible, efficient pricing of energy and network services where it is economic to do so. We recognise that there are advantages and disadvantages to the various options to facilitate and accelerate widespread uptake of the necessary metering technology.

We believe that a contestable model is attractive in principle and the model proposed by the AEMC is worthy of further detailed examination.

However we also recognise that currently the vast majority of mass market meters are owned

and operated by distribution businesses and that advanced metering offers significant potential benefits for networks.

Retailers do not currently provide metering services for types 5 to 7 as part of their retail contracts and in all cases engage the network provider as the responsible person for these types of installations. Currently, the Victorian derogation from Chapter 7 defines remotely read interval meters as type 5 meters to ensure adequate return on investment and prevent meter churn via an exit fee.

We believe that there are sufficient incentives for metering providers to engage in a non-mandated rollout of AMI technology; however they must firstly be adequately defined within the bounds of Chapter 7 based on the technology deployed and the metering charges must be unbundled from the network charges.

To support a competitive metering market the following key components need to be addressed:

- Minimum Functional specifications that cater for both network and retail services;
- Separation of metering charges;
- Access arrangements and service standard that support benefits realisation; and
- Technology neutral platforms and protocols that encourage participation and innovation.

## **Chapter 5 DSP in wholesale electricity and ancillary services markets**

### **Chapter 5 : Draft recommendations Part 1**

A demand response mechanism that pays changes in demand via the wholesale electricity market is introduced. Under this mechanism, consumers participating in this mechanism can either make the decision to continue consuming, or reduce their consumption by a certain amount for which they would be paid the prevailing spot price.

#### **AEMC Questions**

12. Participation in the wholesale market:

- (a) Do stakeholders agree that the proposed demand response mechanism is likely to result in efficient consumption decisions by end-users? If not, are there any changes you recommend to the mechanism to facilitate this?
- (b) On balance, is a new sub-category of market generator required for consumers providing a demand that enables aggregation? What types of issues should be considered when developing the registration process?

13. Consumer baseline consumption:

- (a) What factors should be taken into consideration when developing a baseline consumption

method?

- (b) Have we identified the correct three key principles for developing a baseline consumption method (data refresh, accuracy, metering)?
- (c) Are there any substantial changes to metering and settlement arrangements required for this mechanism to be implemented? Can these issues be resolved through AEMO's consultation process and procedures or are broader amendments to the rules required?

14. Incorporating demand response into central dispatch:

- (a) Do you agree that similar arrangements for generation should apply to demand resources in terms of thresholds for registering as scheduled or non-scheduled basis?
- (b) What are the ways in which the regulatory arrangements can be adapted to facilitate the participation of scheduled and non-scheduled load in AEMO's central dispatch process? Are there any specific changes to reporting, telemetry and communication requirements?
- (c) Should both market and non-market loads above a certain size be required to provide information to AEMO regarding their controllable (and therefore interruptible) load blocks?
- (d) Should there be a trigger in the monitoring and reporting framework that requires consumers to provide greater detail regarding their demand resource to AEMO or affected DNSPs?

**EnergyAustralia response: Do not support**

The draft report recommends the introduction of a new demand side response (DSR) mechanism to pay demand resources via the wholesale electricity market. We understand that the mechanism is targeted at large commercial and industrial (C&I) customers and essentially involves a three way transfer between the customer, retailer and AEMO:

- The DSR participant pays their retailer at their retail tariff against their baseline consumption;
- The retailer settles AEMO at the spot price for the customers baseline consumption; and
- AEMO settles the customer at the spot price times their reduction on baseline usage.

We do not support this draft recommendation as it is unnecessary and inefficient. We believe it would;

- Distort the efficiency of the contract market and investment signals;
- Be complex and costly to implement; and
- Impose costs on all energy consumers for the potential benefit of a few.

We also note that the modelling of benefits of reduced peak demand undertaken for the AEMC by Frontier economic identified the potential benefits mainly relate to networks, and that the benefits in relation to energy are less than the cost of new peaking capacity.

Unnecessary and inefficient

The stated rationale for the DSR mechanism is that ‘in the absence of full cost-reflective pricing, the proposed demand response mechanism may create a similar set of incentives and behaviours with respect to efficient consumption during wholesale electricity market peak and non-peak times<sup>6</sup>’.

However, the wholesale spot market in the NEM already provides efficient, dynamic and real time prices to inform optimal demand and supply responses. The C&I sector is highly competitive and there are no significant technical barriers or market failures that impede efficient pricing of energy for large commercial and industrial (C&I) customers.

The proposal appears to rest on the false assumption that it unlocks economic value that is not already accounted for. The DSR mechanism would create a free option for the consumer to arbitrage between their negotiated retail tariff and the spot price. However, this value is already included in the negotiated retail tariff.

Retailers develop tailored products for C&I customers to meet their consumption profile, risk tolerance and capability for demand response. The value of demand response that a C&I customers is willing and able offer is reflected in their retail tariff. Larger C&I customers can already choose to register with AEMO and be directly exposed to pool prices.

Price volatility is an intrinsic feature of the energy only, gross pool market. Electricity retailers manage price and load volatility for consumers through the contract market. This is not a trivial or low cost risk management service and has significant value for customers and benefits for the market.

The DSR mechanism would distort risk management incentives and inefficiently over value non-firm demand response.

Distort contract markets and investment signals

The draft report suggests that ‘retailers should remain indifferent to a consumer’s decision to enter into a demand response interval ... because consumers continue to pay retailers according to their baseline consumption<sup>7</sup>’. This may appear to be the case on a superficial static analysis. However, a static analysis ignores the impact on forward contract positions, the costs to serve the customer and the increased risks for retailers and generators.

An effective contract market is vital to the efficient operation of the NEM and delivers benefits to all consumers. For example, in a study done for esaa, ACILTasman estimated that a ‘five per cent reduction in contracting across the National Electricity Market could lead to an increase in that retail prices of up to 10 per cent for households, and up to 15 per cent for businesses<sup>8</sup>’.

The DSR mechanism would reduce the ability of retailers and generators to efficiently contract. If

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<sup>6</sup> Draft report pg 62

<sup>7</sup> Draft report Pg 63

<sup>8</sup> [http://www.esaa.com.au/content/detail/national\\_electricity\\_market\\_modelling\\_ACILTasman](http://www.esaa.com.au/content/detail/national_electricity_market_modelling_ACILTasman)

a significant reduction in contracting levels result this would be expected to increase spot price volatility and increase average electricity costs for all consumers.

Under the proposed DSR mechanism, the retailer would settle with AEMO at the spot price for the customer's baseline consumption. To manage the price risk a prudent retailer would need to hedge this load with forward contracts and/or physical generation. However the proposed mechanism would increase risks for generators and undermine the ability of the energy spot market settlement to fund an efficient contract market.

For example, consider a retailer who has a \$300 cap contract with a generator for the DR customer's load. If the spot price is \$1000 and the customer reduces their load below their baseline, the customer would receive \$1000/MWh for each MW reduction below their baseline at settlement. The retailer would seek \$700 / MWh from the generator for their full baseline load. However, at the margin, a generator was not dispatched for the load below the baseline so would not receive spot market income to back the contract.

The draft report identifies that the 'demand response mechanism has the potential to capture between 2100-2800 MW<sup>9</sup>'. If this was achieved, then generators would need to reduce aggregate contract cover by 2100-2800 MW and/or increase contract prices significantly to cover this shortfall risk.

Periods of high prices signal the need for investment in new generation and provide returns to capital invested. It should be remembered that if the scheme was to be successful in achieving a significant reduction in load and pool prices then over time less generation will be built. As noted above, the Frontier economics modelling undertaken for the AEMC indicates that the cost of this demand reduction would be greater than the cost of new entrant generation. We also understand that the DR scheme is intended to be voluntary. However if it does delay investment in new generation, then it would no longer be voluntary.

Average wholesale market prices are more relevant to than the relatively infrequent high price events, and average wholesale market prices, ex-carbon, have fallen in real terms over the last decade and are well below the long run marginal cost of new entrants.

#### Complex and expensive to implement

The draft report does not seek to estimate the implementation costs; we believe there would be significant transaction costs in addition to inefficiencies described above. All retailers would need to alter their billing systems to separate calculation of consumption for billing energy and network charges.

The issues associated with establishing and maintaining baselines are trivialised in the draft report, counterfactual baselines are always imperfect and subject to gaming. The existence of similar schemes in other markets does not demonstrate that they function efficiently. It is worth noting that the incentives for gaming would be very strong, reductions off the baseline may generate short term gains for individual DR participants in excess of 10,000 per megawatt.

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<sup>9</sup> Page 62



If the AEMC is disposed to continue to recommend the introduction of the DSR mechanism in wholesale markets, it should be subject to detailed cost benefit analysis, and comprehensive examination of issues associated with establishing and maintaining baselines.

In the context of forecasting and baselines, it is worth reflecting on the experience forecasting demand in the NEM over the last five years.

#### **Chapter 5 : Draft recommendations Part 2**

The National Electricity Rules (NER) is amended to clarify the Australian Energy Market Operator (AEMO) role in developing both long and short term demand forecasts. This includes estimating DSP, for the purpose of providing accurate price signals to the market over various time frames including pre-dispatch.

To achieve clarity in this regard, the existing rules associated with specific reporting obligations may need to be rationalised to remove any ambiguity regarding their information gathering powers

#### **AEMC Questions**

15. How should AEMO's powers be expanded to improve demand forecasting? Should retailers and other market participants be obliged to provide information regarding DSP capabilities? Will non-obligatory requirements achieve the desired accuracy in reporting requirements?

16. In what ways can AEMO improve its survey questions regarding DSP capabilities? How often should AEMO be required to update its expectations on DSP capabilities in the NEM?

17. Would a pre-dispatch that includes active and price-responsive DSP improve decision making processes for C&I users and aggregators? If not, do you have any other suggestions for improving the ability for AEMO to accurately forecast demand?

#### **EnergyAustralia response: Conditional Support**

Accurate demand and supply forecasts are valuable for consumers and market participants. If there is scope to clarify and simplify existing rules without imposing unnecessary costs on participants we would support this without introduction of a new DR mechanism.

However it is not clear in the draft report what changes are required and what the implications would be. As always, any proposed rule change should be subject to a thorough examination of the costs and benefits.

### **Chapter 5 : Draft recommendations Part 3**

Creating a new category of market participant in the NEM that will allow for the unbundling of all non-energy services from the sale and supply of electricity

#### **AEMC Questions**

15. Do you agree that a new category of market participant should be established for the provision of non-energy services?

16. What types of issues should be considered when developing the registration process, such as eligibility, obligations and liabilities?

17. What metering arrangements need to change to implement this mechanism?

#### **EnergyAustralia response: Do not support**

We do not support the creation of a new participant if that participant could have downstream impacts on existing participants, such as:

- Disconnection of load or part of a load;
- Reduced customer protections; or
- Impact on a retailer's ability to fulfil its contractual or regulatory obligations.

We believe that any participant operating in the NEM who can impact on existing participants and or consumers should be authorised under the NECF as a retailer, distributor or generator. Such authorisations should be structured so that they protect consumers and the market while minimising barriers to participation.

We do not believe that any tiered system should benefit one class of participants over another in relation to similar activities such metering and billing or access to AEMO's settlement system.

### **Chapter 6 Efficient and flexible pricing options**

#### **Chapter 6 : Draft recommendations Part 1**

That governments and industry work together to educate consumers and provide them with the information they need to understand both the system wide benefits and potential individual gains from time varying tariffs

#### **EnergyAustralia response: Support**

Consumer education and information has a significant role to play in the acceptance of time of use

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pricing, and it is important that governments and industry collaborate to ensure its success.

We are committed to helping our customers with efficient solutions for today and tomorrow, and believe that consumers should be empowered to make energy choices that best meet their individual needs. We will work with all our customers, Government's and other stakeholders to help inform and educate energy consumers.

We recognise that Government's, the energy industry and non-government organisations have a role to play to increase energy literacy.

EnergyAustralia has recently launched an exciting new initiative help our customers save energy and money. The 'MyEnergyReport' provides details on customers' home energy use and ways to save money.

MyEnergyReport is an insightful energy saving tool, customers with smart meters will be able to:

- see when they use the most electricity
- compare usage over days, months and years
- monitor daily usage, refreshed every 24 hours
- set up email or SMS bill alerts so you can see how your electricity costs for your billing period are tracking before their bill arrives

**Chapter 6 : Draft recommendations Part 2**

To manage the impacts on vulnerable consumers, we recommend that:

- Arrangements are put in place for consumers, which may a limited capacity to respond, to remain on a retail tariff which has a flat network component. These consumers would have the option to choose a time varying tariff.
- Government programs target advice and assistance to these consumers to help manage their consumption.
- Governments review their energy concession schemes so that they are appropriately targeted.

**EnergyAustralia response: Support**

Consumer education and information has a significant part to play in the acceptance of time of use pricing, and the collaboration of both governments and industry is important to its success.

As an energy retailer we are committed to helping all our customers manage their energy needs, particularly those experiencing hardship.

We also recognise that Government's and consumer groups have an important role in helping all consumers, particularly vulnerable consumers, understand the competitive energy market, their rights as customers, their energy use and how they can save energy and money.

### **Chapter 6 : Draft recommendations Part 3**

The transition to more efficient and flexible price options in the NEM should be done in a gradual phased approach.

We recommend:

- Focusing only on introducing time varying prices for the network tariff component of consumer bills. Retailers would be free to decide how to include the relevant network tariff into their retail offers; and
- Segmenting residential and small business consumers into three different consumption bands and applying time varying network tariffs in different ways:
  - For large consumers (band 1), the relevant network tariff component of the retail price must be time varying. This would require these consumers to have a meter that can be read on an interval basis.
  - Medium to large consumers (band 2) with an interval meter would transition to a retail price which includes a time varying network tariff component. These consumers would have the option of a flat network tariff.
- Small to medium consumers (band 3) would remain on a flat network tariff. These consumers would have the option to select a retail offer which includes a time varying network tariff, if they so choose.

#### **AEMC Questions**

18. Do stakeholders agree with our approach for phasing in cost-reflective pricing? If not, how can the policy be improved to transition to cost-reflective pricing?

19. Have we identified the main issues with transitioning to cost reflective pricing? If not, what other issues need to be considered?

20. How should consumption thresholds be determined?

#### **EnergyAustralia response: Conditional Support**

Enabling efficient pricing requires the introduction of supportive technologies, reform of electricity market rules and deregulation of retail prices. A smooth transition path for small consumers is required to facilitate understanding and acceptance, minimise unintended consequences and allow industry to develop and deploy products and technologies.

We agree support the need for a smooth transition and believe that the transitional approach recommended has merit. The consumption thresholds should nationally consistent and align as far as possible with existing classifications.

Facilitating the smooth and rapid introduction of flexible and efficient pricing is a high priority for energy market reform. It should not be delayed or confused by the introduction of complex new arrangements that seek to partially address the inefficiencies in pricing during transition but will add unnecessary new distortions and complexity.

**Chapter 6 : Draft recommendations Part 4**

Better education and information on the impacts of transitioning to more time varying retail prices.

Each year, distribution network businesses will be required to consult with consumer groups and retailers on their proposed tariff structures.

Amendments to the distribution pricing principles in the NER economic regulation framework are made to better support the introduction of time varying network tariffs.

**EnergyAustralia response: Support in part.**

We support better education and information and amendments to the distribution pricing principles if needed to better support the introduction of time varying network tariffs.

However, consultation between distributors and customers on pricing is inherently difficult. It's also hard to encourage customer interest and understanding of retail pricing.

In our view, the best way to encourage customers to understand pricing trends that affect them is to make network pricing data and trend information more readily available to retailers and bring forward the timing of the publishing of draft network tariffs and approval of these by the AER.

We'd like to see distributors and possibly the AER engaging more with retailers before and during the network price setting process. Some distributors (e.g. Ausgrid, Jemena, Multinet and others) have an annual forum for interested groups to discuss upcoming network price changes. These are useful but if done too late in the process there is a risk that the timing would clash or it wouldn't be impossible to attend all of them. Retailers so informally seek information about draft network tariffs but the information provided is not always reliable.

We support there being greater requirements on network companies to signal their intentions to retailers 3-4 months prior to the tariff changes effective date on the following:

- new tariffs – including calculation rules, structure details, approximate price level, applicability and method/timing of use with customers
- tariff reassignments affecting more than 5% of any tariff group
- structure changes to existing tariffs – including structure details, approximate price level
- deviation from the price path

**Chapter 6 : Draft recommendations Part 5**

The distribution network pricing rules in the NER are amended so that distribution network businesses have sufficient guidance to set efficient and flexible network tariff structures that support DSP.

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A new provision is included in the rules which require distribution network businesses to consult with consumer groups and retailers on their proposed tariff structures each year.

**EnergyAustralia response: Support**

**Chapter 6 : Draft recommendations Part 6**

Once a residential consumer has a meter which measures on an interval basis (ie every 30 mins), that consumption should be settled in the wholesale market using the interval data and not the net system load profile. This will be the case irrespective of whether the consumer has a flat retail tariff.

**EnergyAustralia response: Support**

We support the recommendation; it is our understanding that this reflects the status quo.

**Chapter 7 : Distribution network incentives and distributed generation**

**Chapter 7 : Draft recommendations Part 1**

The AER consider reforming the application of the current demand management and embedded generation connection incentive scheme to provide an appropriate return for DSP projects which deliver a net cost saving to consumers. We have put forward principles and two mechanisms for how this could be achieved.

**AEMC Questions**

22. Would it be beneficial to include reference to the suggested mechanisms and provide more guidance and an overall objective in the Rules governing the demand management incentive scheme?
23. Should separate provisions for an innovation allowance be included into the rules? Given that the costs of the allowance would be borne by electricity consumers, is it more appropriate for such innovation to be funded through government programs?
24. Should the provisions for a demand management incentive scheme be included in the regulatory framework for transmission businesses?

**EnergyAustralia response: Conditional support**

Regulation of network businesses should provide efficient incentives to optimise demand side options. However it is also important ensure competitive neutrality and appropriate ring fencing if network DSP is competing with unregulated options.

**Chapter7 : Draft recommendations Part 2**

A two-part approach is adopted to address the issue of business profits being dependent upon actual volumes. This includes improvements to the pricing principles to guide network tariff structures and secondly, to include an allowance for foregone revenue under the DSP incentive scheme.

**AEMC Questions**

25. What amendments are required to the current distribution pricing principles as set out in clause 6.18.4 of the national electricity rules?

**EnergyAustralia response: Conditional support**

Regulation of network businesses should provide efficient incentives to optimise demand side options. However it is also important ensure competitive neutrality and appropriate ring fencing if network DSP is competing with unregulated options.

**Chapter 7 : Draft recommendations Part 3**

We recommend that the NER is clarified to enable the AER to consider potential non-network benefits when assessing the efficiency of network expenditure allowances.

We recommend that the NER is amended to include the ability for distribution network businesses to have extra flexibility in their annual tariff setting process to reflect changing DSP costs.

We propose that a new rule is introduced in the NER that provides distribution network businesses with more certainty on how DSP expenditure incurred in a regulatory period (but which is not included in the approved allowance) will be treated in future regulatory determinations.

We propose that the NER is changed to permit the AER to grant temporary exemption from reliability service standards for specific DSP pilots/trials.

We recommend that the AER should give consideration to the benefits of allowing distribution network businesses to own and operate DG assets when developing the national consistent ring fencing guidelines for these businesses

We consider that SCER should, in developing a national approach to feed in tariffs, take into account the value of time varying feed in tariffs to encourage owners of DG to maximise the export of their energy during peak demand periods

**EnergyAustralia response: Conditional support**

Regulation of network businesses should provide efficient incentives to optimise demand side options. However it is also important ensure competitive neutrality and appropriate ring fencing

if network DSP is competing with unregulated options.

In particular incentivising network companies to export energy from their distributed generation assets is likely to distort the energy market and may contravene competition principles.

## Chapter 8 – supply chain interactions

### **Chapter 8 : Draft recommendations Part 1**

The recommendations are a package of integrated reforms for the market. If implemented, the market should have time to adjust and transition to the new environment. There should be ongoing monitoring and evaluation of the market for the desired outcomes to be achieved. We therefore do not consider that additional regulatory mechanisms beyond those recommended in this report are needed for the market at this time.

### **EnergyAustralia response: Conditional support**

We no additional measures should be considered, however not all measures canvassed should proceed.

## Chapter 9 Energy efficiency policies and measures

### **Chapter 9 : Draft recommendations Part 1**

There is better coordination of energy efficiency and DSP policy and measures.

Any regulatory schemes relating to energy efficiency need to address the secondary impacts that they are likely to have on the electricity market and its participants.

There is better reporting and more publicly available data on the load shape impacts of energy efficiency measures on both peak and average electricity demand.

### **EnergyAustralia response: Support**

Consideration of the design and the cost and benefits of energy efficiency schemes should be cognisant of the fact that they operate in a competitive national market. It is important that such schemes, including the mooted national energy savings initiative, be subject to regular and robust regulatory impact assessments against clearly defined objectives, and should only be introduced or retained where they can clearly demonstrate a significant net benefit.

NEM jurisdictions with energy efficiency schemes should ensure maximum harmonisation with other jurisdictions, particular in respect to compliance for retailers and requirements for activities.



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The introduction of carbon pricing, together with dynamic cost reflective pricing, will provide better incentives to optimise DSP and encourage a strong energy services industry. This is likely to reduce the benefits and justification for standalone energy efficiency schemes.

We consider that the differing objectives and lack of coordination between the existing schemes are likely to act as a barrier to the integration of DSP. In considering whether peak demand objectives should be included energy efficiency schemes care should be taken to ensure that the benefits are not outweighed by the increase in complexity and compliance costs.

Generally speaking, activities accredited under energy efficiency schemes do not require interval data, as a reduction in total consumption provides consumers with the necessary price signals to take action.