



EnergyAustralia

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Dear Commissioners

Draft Determination – Demand Response Mechanism and Ancillary Services Unbundling

EnergyAustralia is pleased to make this submission to the Australian Energy Market Commission's (the Commission) Draft Determination on the Demand Response Mechanism and Ancillary Service Unbundling rule change proposal. We are one of Australia's largest energy companies with over 2.5 million electricity and gas accounts in NSW, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own and operate a multi-billion dollar energy generation portfolio across Australia, including coal, gas, and wind assets with control of over 4,500MW of generation in the National Electricity Market.

EnergyAustralia welcomes the Commission's decision to narrow the scope of the initial rule change proposal and exclude the Demand Response Mechanism (DRM). This decision recognises that the industry has evolved since the Commission completed its Power of Choice review on 2012 and that some of its specific recommendations are no longer required. This is a pragmatic approach that reflects market reality.

The volume and variety of demand response (DR) in the market continues to grow as a function of the flexibility of business practices, technological change, greater customer engagement and competition between retailers. The Commission has undertaken comprehensive analysis and documented this well in its Draft Determination.¹

We see a greater interest in demand response with the return of volatility and higher prices in wholesale markets across the National Electricity Market. We stated in our previous submission that the wholesale market context is important when assessing the current level and potential for DR.² The frequency of extreme price events – and their duration and predictability – and overall level of prices was relatively low when the Commission commenced its consultation. This may explain the concerns of some stakeholders about the observed level of DR at that time and their support for the DRM.

¹ Australian Energy Market Commission (2016), *Draft Determination: Demand Response Mechanism and Ancillary Services Unbundling*, pp. 17 - 18

² EnergyAustralia (2016), Submission to AEMC Consultation Paper

Competition creates strong incentives for retailers to explore DR options with their customers and for customers to seek out retailers and other market participants who can satisfy their requirements or offer advice about the optimal form of DR for their business. Furthermore, we see few obstacles to customers switching retailers if their current retailer is not willing to consider an arrangement that satisfies their requirements, including DR arrangements that are tailored to their business. As the Commission notes, regulatory developments following on from its Power of Choice review (such as cost reflective network tariffs, competition in metering, and customer access to data) will complement the competitive market, enabling more customers to better manage their energy consumption and to receive a commensurate benefit.

Within this context, supporters of the DRM component have failed to make a convincing case that there is significant and unrealised DR in the market. The perceived barriers are either theoretical, do not reflect retailers' true incentives (which are to retain and win customers by offering retail products that reflect their needs rather than selling large volumes of energy), do not take account of the broader wholesale market context or have dissipated over time.

We also welcome the Commission's comprehensive analysis of the negative impact and less effective elements of the specific DRM proposal. In particular, we agree with the AEMC on the following:

- Spot prices would not reflect competition from DR as it would be self-scheduled by the new market participant, and therefore, not included in central dispatch.
- The DRM would require costly changes to the wholesale market and retailer systems (the estimated value of those costs seems reasonable).
- The DRM would not necessarily alleviate network constraints and defer network expenditure as wholesale market prices do not necessarily coincide with network peak demands.
- The DRM could have unintended consequences and create distortions in the spot market and related markets:
 - less reliable self-scheduled demand response resources would be rewarded under the DRM in an equivalent manner to more reliable, firm scheduled resources in the spot market.
 - retailers that participate in the DRM would continue to be financially responsible for their customers' baseline consumption so an outcome of the DRM may be that customers pay for a retailer's hedging costs through their retail contract even if they provide demand response.
 - hedging contract prices are likely to increase. Demand would remain the same as retailers would continue to remain financially responsible for the baseline consumption of their customers but supply is related to generation, which will be at the levels of actual consumption.

Frequency Control Ancillary Services

We see little need to proceed with the creation of a new type of market participant – market ancillary service provider – to offer a customer's demand response, or aggregation of customers' demand responses, into frequency control ancillary services (FCAS) markets. As

with the DRM proposal, we do not see significant *market* obstacles to customers offering their load to FCAS markets but rather, view the current level as a function of regulatory and technical requirements. The proposed rule does not address these issues so we expect an expansion in FCAS attributable to the proposal will be small and therefore, any incremental benefits may not outweigh implementation costs.

More fundamentally, the evolution of the NEM – through the diversification of energy sources and the decentralisation of generation, for example – and recent events in South Australia confirm the need for policymakers and regulators to reassess the incentives for market participants to provide the complete range of support services (through DR of some other mechanism). This might be through the creation of an inertia market, alignment of settlement and dispatch, or more fundamental changes to wholesale market design. The proposed rule change might be redundant in this context.

Should you require further information regarding this submission please call me on (03) 8626 1242 or Geoff Hargreaves on (03) 8628 1479.

Yours sincerely

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