

Australian Energy Market Commission
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Distribution Market Model Draft Report

The Australian Energy Council (the Energy Council) welcomes the opportunity to make a submission to the Australian Energy Market commission's (AEMC's) Distribution Model Draft Report (the Draft Report).

The Energy Council is the industry body representing 21 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia and sell gas and electricity to over 10 million homes and businesses.

The Energy Council considers that the co-optimisation of the use of distributed energy resources (DERs) across multiple potential markets should be the goal of any market or regulatory reforms. Accordingly we agree with the AEMC's framing of this goal as one of optimisation and co-ordination, which are the two components of co-optimisation.

Co-optimisation requires a level playing field for the development of different distribution markets

The multiple value streams identified by the Draft Report (as per Figure 2.2) encompass a range of customer, network and wholesale services. Only customers can determine what value they place on customer services, and for this reason alone, customers must be at the centre of distribution markets. This entails them having ultimate control of how their DERs are utilised. In practice, most customers and small customers in particular are unlikely to be interested in devoting their time to direct control of DERs or co-ordination of different uses. Accordingly, we expect that customers will effectively "sell" control of their DERs to the party who can best optimise and co-ordinate use of the DER. In order to maximise competition, the benefits in the other types of markets identified by the AEMC (markets for wholesale and network services) must be accessible to all parties and on equal terms. This has consequences for various aspects of network regulation, including tariff-setting, ringfencing, regulatory investment tests and access to network capacity and performance data. These issues are addressed in greater detail in our rule change proposal *Amendments to Chapters 5, 6, 6A and 7 of the National Electricity Rules In the implementation of Demand Response and Network Support Services*¹.

¹ <http://www.aemc.gov.au/Rule-Changes/Contestability-of-energy-services-demand-response>

The most substantial piece of work in the Australian energy market context relating to distribution markets is the ENA/CSIRO roadmap (“the Roadmap”). This report does an excellent job of identifying the potential scale of the benefits to consumers from the development of efficient and effective distribution markets. As should be expected from a report sponsored by the peak body for Australian energy networks, the Roadmap takes a somewhat network-centric approach to distribution-level markets. Accordingly, we consider that the Roadmap does not fully address the issues of co-optimisation with non-network services. Additionally the roadmap is clear on *what* distribution markets (in particular their proposed Network Optimisation Markets) look like than *how* we get there. With these points in mind, the Energy Council commissioned KPMG to carry out some analysis of the Roadmap and the issues that may arise that are not addressed (or not fully worked through) in the Roadmap. We attach the KPMG report (Distribution Market Models: Assessment of Supporting Frameworks) as part of our submission.

KPMG identify three key risks:

1. The ability of DER to be co-optimised across multiple value streams could be constrained.
2. The ability of DNSPs to procure DER directly from customers is likely to impede the development of competitive DER markets and limit the ability of DER to capture the full value of its services.
3. Potential conflict of interests for the DNSP, especially if the distribution system operation role remains integrated within the distribution network service provider

Cost reflective tariffs are important but not the only consideration

To ensure all parties can access the benefits that DERs can provide to the network, price signals are required. The most obvious route to these is via cost-reflective tariffs for use of the network. This point requires further unpacking.

Under the current framework of pricing network services to individual customers there is already a proliferation of different network tariffs for small customers. In the short term at least, the development of more cost-reflective tariffs such as demand tariffs adds to this proliferation because cost-reflective tariffs are effectively offered on an opt-in basis. This is a consequence of the interaction of the requirement that customers must choose if they would like a more advanced digital meter if they do not already have one and the fact that such meters are required to appropriately settle these new more cost-reflective tariffs. In Victoria where digital meters are ubiquitous it is by regulatory fiat. So tariff design will be more effective where it creates a strong incentive or customers to agree to the installation of a digital meter because there are clear financial benefits to them in doing so.

Retailers’ experience is that most customers value simplicity in tariff design. It is neither necessary nor desirable for all network tariffs to be passed through in order for the price signal to be effective. As long as the retailer is exposed to the price signal and has the freedom to appropriately manage the risks of a difference between the network tariff structure and the retail tariff structures their customers choose, that is enough. Tariff structure pass-through is a legitimate risk management approach to be sure, but not the only one. The same applies to other aggregators who are already entering the market via service offerings based around DERs (e.g. Reposit). After all, another major component of household electricity bills, the wholesale energy cost, is not directly passed on to

most customers. Instead it is settled in aggregate for each retailer's total customer load and most customers appear content with simple structures rather than opting to be exposed to real-time spot prices. Yet the energy market is not considered to be a failure because of this feature.

Cost-reflectivity applies in principle to export tariffs for energy (and potentially other costs/services) as well as import tariffs. Recent jurisdictional reviews have sought to consider the applicability of greater cost reflectivity export (feed-in) tariffs in isolation, which satisfies neither efficiency nor fairness criteria. This is clear from the AEMC's analysis of customer services provided by DER, as this includes retail tariff arbitrage. In this context we are supportive of the AEMC's proposal to explore deleting clause 6.1.4 of the NER, without prejudice to whether deletion is the best outcome at this point.

Locational price signalling is another element of true cost-reflectivity. Yet the political and social acceptability of this economic logic appears very weak. Different prices arising from customers living in different distribution network areas in the same state are periodically held up as unfair, and more than one jurisdictional government has a long-standing policy of equalising prices for metropolitan and regional areas despite the significant underlying cost drivers. Promoting absolute cost-reflectivity, for example through highly granular nodal pricing, may not deliver efficiently benefits if retailers are constrained by public opinion from taking any meaningful action to manage their risks. Fortunately there are other ways to send price signals on a locational basis, including via a call for non-network solutions as part of a Regulatory investment test process. Many networks are already doing this effectively, including creating opportunities for aggregators to bundle up demand response from multiple customers whose loads are too small to meet the networks' minimum threshold. A key challenge for the industry is to convert these periodic calls for non-network solutions into an ongoing two-way process. It is not clear at this stage whether policymakers and regulators need to take specific actions to help foster the development of this market, but at least a monitoring role to ensure a level playing field and that networks faced balanced incentives for network versus non-network solutions would be worthwhile.

Connecting DERs

Businesses offering DERs and services from DERs are likely to operate across multiple distribution areas. The development of these markets would thus be supported by ensuring a consistent approach to connecting DERs. Accordingly we support the AEMC reviewing the technical connection standards with a view to streamlining and harmonising connection processes. We do not consider there is a need at this stage to explore deeper connection charges.

Any questions about our submission should be addressed to me by email to kieran.donoghue@energycouncil.com.au or by telephone on (03) 9205 3116.

Yours sincerely,



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