AUSTRALIAN
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COUNCIL

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Unlocking CER benefits trough flexible trading – Consultation Paper

The Australian Energy Council (AEC) welcomes the opportunity to comment on the consultation paper – Unlocking CER benefits through flexible trading.

The Australian Energy Council (AEC) is the peak industry body for electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. Our members collectively generate the overwhelming majority of electricity in Australia, sell gas and electricity to millions of homes and businesses, and are major investors in renewable energy generation. The AEC supports reaching net-zero by 2050 as well as a 55 percent emissions reduction target by 2035 and is part of the Australian Climate Roundtable promoting climate ambition.

The AEC response to the consultation is provided below. In addition to the AEC response, the Australian Energy Council (AEC) commissioned Oakley Greenwood (OGW) to prepare an independent response to the AEMC's Consultation Paper. OGW has developed its response based on fundamental principles of economic efficiency and the National Electricity Objective (NEO), and provide independent views. OGW have had full control of the document including final editorial control. The OGW report is also attached.

The rule change request

AEMO's rule change request puts forward that by separating flexible and inflexible loads, consumers could access more value from their CER - including through better access to incentives for their CER to support the market and power system operation. To examine this hypothesis, it is important to understand what types of value consumers may be looking for from their CER and what motivations and preferences influence their choices to take up CER or related offers, so that we can assess the potential benefits from flexible trading.

The perceived problem is that small customers are limited in selling their exported excess generally to the retailer they use for their energy supply. The proposed solution is to expand the trading relationships available at a single supply point. The matters to be addressed are:

- Are there any real consumer benefits in this, and;
- Do the benefits outweigh the costs of the required changes.

Are there any real consumer benefits?

There are orchestration options available to customers now. Virtual Power Plants (VPP's), the Wholesale Demand Response Mechanism (WDRM) and the Small Generation Aggregators (SGAs) provide that framework and there is no shortage of markets or potential opportunity in the current governance structures. There is however a relatively trivial participation and response, caused by both nascent technology that is yet mainstream, and that also that in normal periods energy prices will usually be below the willingness-to-pay of almost all loads. The attached Oakley Greenwood report (the report) notes that it is primarily behind-the-meter batteries that, if orchestrated, could generate material economic benefits but that up until recently, there has only been a limited stock of batteries to orchestrate. This latter point means that we should not have expected the market to have arranged itself in a way that focused on 'controlling/orchestrating' lower value CER devices (other than batteries or perhaps EV's, of which there are also not many) because the economics did not stack up. This seems like economic theory working in practice rather than a market design issue.

The consultation hypothesis is that CER customers are not receiving the full value for their contribution to market and power system operation. However, there are multiple retailers to choose from and a logical conclusion would be that in such a competitive market that CER value would be accounted for. Bundling is attractive to consumers who benefit from a single, value-oriented purchase of complementary offerings. Bundling helps to increase efficiencies, thus reducing marketing and distribution cost. And it allows the consumer to look at one single source that offers several solutions. It should be instructive to the consultation that after the expense, complexity and risk of establishing the WDRM, that Enel X[1], while being a DRSP and offering DR also has a retail licence, allowing it to bundle its services.

Retailers provide an overall package incorporating the benefits and the risks of the customer CER. Assigning that value elsewhere via an additional trading relationship does not necessarily change the CER customers overall position, as the retailers, distributors and metering coordinators fixed costs per customer do not change, and would logically increase to recover costs associated with the change; but the new fixed costs from the second and subsequent providers must now also be met. This outcome in part is why, in competitive markets, the bunding of products and services is most likely to lead to lower overall costs for consumers as fixed costs are spread over a wider suite of products and services. For example, a bundled house and home contents package is likely to be better value than two independent policies from different parties.[2] Similarly with bundled gas an electricity, which has significant penetration not only as a single bill product, but also as two separate accounts where savings are applied for having both with the same retailer.

The obligations to vulnerable customers for life support are also glossed over in the proposal. Life support appliances include the like of air conditioning and hot water; which are also the subject of the partitioning proposed by AEMO. If the provider of life support services is not a retailer, then the consultation needs to better consider how those critical obligations will be applied to non-retailer FRMPs. There will also be impacts on hardship, best offer notifications and even the DMO/VDO. The premise that the proposed changes will only be material for those who wanted to offer FTA services and do not impact on retailer operations significantly in terms of functional and technical specifications of billing, forecasting and pricing is at this stage neither tested nor credible.

Beyond these practical considerations, the AEC commissioned Oakley Greenwood report examines the different potential economic values associated with orchestrating different CER devices. This to date largely absent but important consideration helps explain why the market has developed as it has up until now and provides useful insight into how the market is likely to naturally evolve in response to the rapid (forecast) take-up of certain types of CER. It is behind the meter batteries that can generate material benefit s with other CER devices provide only marginal economic benefits. Now that we are seeing a greater penetration of batteries, we are also seeing a clearer interest in VPPs and CER orchestration.

The barriers to entry identified in the consultation appear to largely be consumer protection, and in terms of consumer benefits this needs serious examination as to what specific characteristics of controlled loads make them justifiably less essential than others? Perhaps EV's, with their public charging alternatives and transport not being a historical electricity essential could make a discrete consumer protection case the costs will be real, and the benefits highly uncertain.

Do the benefits outweigh the costs of the required changes

Given the requirements of the NEO and given the scale and impact on the industry of the proposed change, a detailed cost benefit analysis (CBA) should be done prior to any Rule change being made[3]. In politicised contexts, the Cost Benefit Analysis (CBA) method can (and has) been used for justificatory rather than for evaluation purposes. Some CBA's do require that net qualitative benefits are judged to outweigh the net financial costs, but in this specific case/s the benefits are capable of being reduced to financial terms and proper evaluation could be conducted. This should also include assessment of what is likely to happen

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[1] Enel being the single participant of its type

[2] Noting that this example is a much easier accounting and financial settlements proposition than that proposed by AEMO.

[3] Oakley Greenwood identify this in their report.

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absent any change, which in our preliminary view is the approach most likely to provide the greatest surplus of benefits over costs as the market arranges itself efficiently.

Compared to similar changes borne from the introduction of new market participants/transactions the AEC estimates that individual retailer costs of up to $30 million are plausible. Bear in mind that Power of Choice implementation cost individual retailers amounts in the order of $60 million.[4] Of course costs can be justified if there is a benefit. But as Oakley Greenwood note in their report, the lack of partnering with CER aggregators historically may have had nothing to do with misaligned incentives between the retailer and their end consumers presupposed by the proponent and the AEMC's consultation paper, and more to do with the underlying economics of aggregating the types of CER that were available at the time the opportunity arose.

Conclusion

The report observes that the market appears to be much more aligned in its view that there is a clear sustained increase in the number of batteries being installed as well as the number of EVs being purchased, and therefore as to the likely penetration and therefore the potential value proposition related to the market's use of these CER devices in the future. The market is now likely to naturally evolve in response to the rapid forecast take-up of these types of CER which will significantly change what a 'typical' retail customer's load profile looks like, and the types of products and services that retailers will offer. The consultation must therefore explicitly consider how the retail market is likely to evolve under the business-as-usual case.

The AEC agrees with the reports assessment that the rule change proposed does not represent a solution to an actual problem that will occur in the future, but rather is a solution to a perceived problem from the past, based upon a misunderstanding as to why the market has developed in a certain way until now.

Please contact the undersigned at david.markham@energycouncil.com.au should you wish to discuss.

Yours sincerely,

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[4] The AEC spoke to retailers about retailer costs but given functional and technical details are vague, this early comparison is the best guide for now.