Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Submitted online at: www.aemc.gov.au
22nd December 2015

To whom it may concern

The Alternative Technology Association (ATA) welcomes the opportunity to provide feedback to the AEMC's Consultation Paper regarding the Demand Response Mechanism Rule Change.

We thank the AEMC for preparing a very useful paper and for their endeavours to include consumer advocates in this very important process.

ATA

Founded 35 years ago, the ATA is a National, not-for-profit organisation whose 5,500 members are residential energy consumers.

Through the application of our experience in energy policy and markets to our advocacy and research, and close collaboration with fellow members of the National Energy Consumer Roundtable, the ATA is an important voice for energy consumers Australia-wide.

ATA presents a uniquely two-fold perspective as a consumer advocate: with the continuing support of the Consumer Advocacy Panel (now Energy Consumers Australia) we represent the interests of all small energy consumers in with respect to the promotion of energy affordability and improvements to the NEM, and speak with authority on behalf of the growing portion of the consumer base who have an active interest in demand side participation.

Commentary

In ATA's view, the Demand Respond Mechanism is equal only to improvements to network pricing as the highest priority of the Power of Choice reforms. Hence ATA has been very closely involved throughout the DRM rule change development process.

OGW's Cost Benefit Analysis of the DRM compared a low estimate of the benefits with a liberal estimate of the costs, and **still found a net benefit for all consumers**. For this reason alone, introducing the DRM in the NEM is what is commonly termed as a 'no-brainer'. In preparing this submission, ATA turned to the internet to find a similarly common term to best capture why the DRM reform still remains uncertain in spite of SCER having accepted the AEMC's sensible recommendation to implement it in 2012. We didn't find one, but the search yielded some food for thought.

When Googling the words '*incumbent industry too much influence*', the first search result is - by sheer coincidence - a 2009 US publication entitled *Competitive Electricity Markets: The Power of*

Choice[1]. On page 37, Authors Joseph L. Welch and C. J. Bolling reflect on competitive energy market reforms in the US:

> *'In too many states, the industry reform debate was soon deflected into tertiary issues or otherwise wrong minded ideas. A* ***No-Loser Test*** *became popular, in which it was predicated no incumbent participant should be harmed in the process of industry reform. And as conciliation became an ever important driver to restructuring, the core tenets of policy reform were gradually overpowered. Rather than simply describing the end-state competitive policy environment, volumes of legislation grew around sheltering industry incumbents from potential losses*[2]*.'*

Welch and Bolling go on to discuss the disproportionate magnitude of resources that incumbent businesses could devote to lobbying against changes that threaten their profits, compared to lack of resources which proponents (consumer advocates, prospective new entrants and some academics) have to lobby in favour of reforms. They also consider the barriers to good reform outcomes posed by some states.

There are many striking similarities between Welch and Bolling's perspective in the US and ATA's experience with the DRM rule change process, from AEMO's initial ill-fated DRM rule change proposal, right up to the current revised DRM proposal. These include the role of a jurisdictions (one that is dependant on revenue from state-owned generation infrastructure) in undermining the reform; that incumbent lobbying power has clearly displaced the long term interests of consumers; A *No-Loser Test* effectively has effectively been applied in making decisions about the DRM design in allowing retailers to actually prevent consumers from participating in the DRM; the same concession to retailers thereby eroding the core tenet of the Power of Choice reforms: that consumers (not retailers) should have more choice.

OGW's Cost Benefit Analysis of the DRM for COAG Energy Council compared a questionably low estimate of the benefits of a DRM with incumbent energy business' liberal (and to this date entirely unsubstantiated) estimate of the costs of DRM, and, as noted above, still found a net benefit for all consumers. Given this, allowing any retailer to restrict any consumer from participating in the DRM, represents an unambiguous failure to prioritise the long term interests of all consumers.

In ATA's 2012 submission to the Power of Choice directions paper, we called for the primacy of the NEO to be restored, observing that:

> *'… particularly at the level of policy design and implementation, the energy market has failed in many ways to achieve the NEO. In our view, the NEM has often been more*

[1] https://books.google.com.au/books?id=iiRVAgAAQBAJ&pg=PA37&lpg=PA37&dq=incumbent+industry+too+much+influence&source=bl&ots=ObjMnV_z_g&sig=mtcT_1G9zSJQMElQsTWcPGX-Y0Y&hl=en&sa=X&ved=0ahUKEwj7ipfazNzJAhUJJZQKHYmeAOAQ6AEIHDAA

[2] Authors' spelling mistakes have been corrected herein

> *successful at protecting the long term interests of a number of market participants and network service providers than it has of protecting the long term interests of consumers.'*

In recommending the DRM to SCER as part of the Power of Choice reforms, the AEMC certainly put the long term interests of consumers first. This DRM rule change presents the AEMC with another opportunity to restore the primacy of the NEO.

Key recommendations

ATA asks that the AEMC remains steadfast in putting the long term interests of all consumers first, by

- **Considering 'voluntary' DRM options that do not prevent a consumer from participate in DRM.** ATA understands the decision by Energy Council to allow retailer's participation to be 'voluntary' is a concession that has been important in reaching accord among COAGEC in progressing the DRM, after retailers expressed concern about the need for system upgrades that relates primarily to the baselining and 'split settlement' of billing/wholesale and network costs. ATA agrees there is value in implementing the DRM in a way that manages the costs for retailers. This can - and in our view, must - be done without creating unnecessary barriers to consumers participating in the DRM: 'Voluntary' must not be interpreted to simply give retailers the ability to refuse a customer from participating in a DRM.

- **Disregarding the (still entirely unsubstantiated) claims of implementation costs made by incumbent retail businesses**, or at least requiring some evidence of the validity of these claims.

- **Implementing the DRM at the earliest practical opportunity.** There need be no material cost to energy businesses under the 'voluntary' model, hence no benefit in deferring this stage of the DRM reform for any longer than it takes AEMO make their necessary changes.

- **Moving to a 'non-voluntary' model by the end of 2018.** That will present ample opportunity for retailers to prepare their systems for DRM as they undertake deep systems changes for other reforms, such as metering reforms and the introduction of cost reflective network pricing.

All the above matters are further explored further herein, along with ATA's response to questions raised in the discussion paper.

Question 1 Assessment Framework

1. Would the proposed framework allow the Commission to appropriately assess whether the rule change request can meet the rule making test?

2. What changes to the proposed assessment framework would stakeholders' consider appropriate, if any?

1.1 and 1.2

In ATA's view the proposed framework is a good starting point but requires some minor improvements to better achieve the NEO.

Proposed outcomes

Of the four proposed outcomes, ATA suggests the following changes:

- Assist in determining the lowest cost dispatch of scheduled electricity load, generation and ancillary services in order to balance supply and demand;

In ATA's view this outcome should expressly have regard to the longer term outcomes, and in application should it take into account the pace of reform.

Why is this important? Currently the NEM is oversupplied with generation, and wholesale prices are low, which some view as lessening the immediate need for a DRM. In ATA's view, the opposite is true: there is no better time to implement the DRM, as:

- The wholesale market does not require demand growth to support effective participation: it requires price volatility. We are seeing significant generation retirements already, along with a slowing of demand reductions, returning price volatility to the market.
- The dramatically inaccurate demand forecasts that have contributed to the current oversupply of capacity are unlikely to be repeated, and energy businesses are placing less stock in them in any case.
- It is impossible to know what the electricity system will look like in the longer term: technological and economic shifts may lead to any number of disparate supply/demand scenarios. Under some scenarios, peak demand would increase, and under most scenarios, given the growing role of variable renewable energy generation, price volatility would increase.
- In the context of this heightened uncertainty, increased DR participation will be extremely valuable, as it will may avoid the need to build new peaking generation. Arguably, if a DRM had been implemented in the early 2000s, when wildly inaccurate forecasts led to overinvestment in generation infrastructure, billions of dollars of capital expenditure (in the generation and network sectors) would have been avoided.

- The reform process is slow. The current incarnation of the DRM was first proposed by the AEMC in 2012 and it looks like the soonest it could now be practicably be implemented is 2017. It will then take at least 2 years for a competitive DR market to develop. If we defer a DRM until we urgently need more DR, our response is again likely to be too late to avoid unnecessary capital spend.

> • Incentivise electricity users to make decisions to use electricity at times when the value of its use exceeds its underlying cost;

In ATA's view this outcome should be framed in the reverse – the objective is to incentivise energy users to **use less energy at times when it's underlying cost exceeds its value** to that user.

Proposed factors

Of the three factors identified by the AEMC in relation to understanding whether the rule change making test should be passed, ATA suggests amending two:

> • Whether the costs and benefits are allocated to parties that are best able to manage them; and

This needs to reflect that some benefits are not 'managed' per se, but 'accrue' to parties. For example, **the benefits that accrue to participating consumers (including the wealth transfer from generators to participating consumers) should be considered in the context of the costs and benefits to consumers.**

Improvements to the market signal

ATA questions the below interpretation of the impact of DRM on the market's competitive process.

> • **Impact on the market's competitive process**: Whether the DRM mechanism design could establish and maintain a level playing field between competing technologies for generation and demand response resources to balance supply and demand in peak time periods, in a way that avoids the risk of the mechanism biasing the market's technology choices and displacing more efficient technologies for less efficient ones.

As noted previously, if a DRM had been implemented in the early 2000s when wildly inaccurate forecasts led to overinvestment in generation infrastructure, billions of dollars of capital expenditure may have been avoided.

The notion that the DRM could potentially introduce technological inefficiencies appears unusual, given that

- major technological inefficiencies exist now due to the supply side bias from the lack of such a mechanism.
- There is little apparent new technology risk introduced by the DRM, which involves switching off loads rather than investing large amounts of capital in generation.

ATA recommends reframing this assessment of the impact of the market's competitive process to also consider the capacity of DRM to displace less efficient technology choices with more efficient ones.

Question 2 Potential barriers to demand side participation relevant to this rule change request

1. What are stakeholders' views on the potential barriers to demand side participation that have been set out in this consultation document? How relevant might they be? Should they be considered in the Commission's assessment?
2. Have stakeholders identified other barriers to DSP that should be considered in the Commission's assessment? Please, explain and provide evidence where possible
3. What are the costs and benefits of removing the barriers that are identified as significant to this rule change request? Which barriers are the most problematic and/or more cost-effective to remove?
4. Are there any current or upcoming changes in the market that would mitigate or address any of the identified barriers?
5. Might there be any unintended consequences from addressing such barriers?

2.1

Yes, all barriers to DSP should be considered in the commission's assessment.

2.2

The main barrier is that retailers see DR as a competitive threat to the generators which they contract with or own.

Another major barrier to Demand Side Participation in the wholesale market is that many large consumers are in long term retail contracts for the sale of energy with their retailer. Competition in DR is therefore all the more restricted because customers can only sell DR to the retailer they buy

their power from. Customers choose retailers mainly on the basis of energy prices, so there is little competitive pressure on retailers to offer DR deals. To be effective a DRM will ultimately need to allow consumers to contract with a DRA regardless of their retail contract.

Another barrier is that there is a lack of specialist aggregators competing with retailers for customers' DR capabilities. A DRM will help to overcome this.

2.3

Other opportunities for removing these barriers include awkward retail regulation measures (like requiring all retailers to offer selective spot price pass-through options for large consumers) or fundamental changes to energy market arrangements (like disaggregating retail and generation). These opportunities appear much more costly than implementing a DRM.

2.4

No.

2.5

None that are materially detrimental or unacceptable. The consequences of not addressing these barriers is far greater than the consequence of not doing so.

Question 3 Questions on the overall DRM design proposal

1. Would the proposed DRM generate useful demand-side information in relation to improving wholesale pre-dispatch and dispatch prices? How significant would this improvement be?
2. Would the proposed DRM generate useful demand-side information in relation to improving the management of transmission constraints through the dispatch process? How significant would this improvement be?
3. Would the proposed DRM generate useful demand-side information in relation to improving the provision or procurement of ancillary services? How significant would this improvement be?
4. Would the proposed DRM operation result in a technology neutral approach between demand response and generation resources?
5. Do stakeholders think that there exist any relevant gaming risks or unintended consequences from implementing the overall proposed DRM operation? If so, how could they be mitigated in a cost-effective way?
6. Would the DRM result in system-wide benefits and/or costs that might impact the operation and investment in electricity transmission and distribution networks? What aspects of the design would contribute to this?
7. Would the DRM result in improved ability for AEMO to manage system security and reliability? What aspects of the design would contribute to this?

3.1, 3.2, 3.3

Currently the scale and behaviour of DR is largely unknown to the broader market, as most of it occurs in off-market arrangements and the remainder that is exercised by or for market customers is done without notification. If an effective DRM were introduced, existing DR customers are likely to participate, improving the demand side information provided.

3.4

An effective DRM would improve the 'technology neutrality' of the NEM. The 'voluntary' DRM proposed is not strictly technology neutral, as it provides incentive for retailers to continue to

choose supply side generation technology over demand side participation options, but would nonetheless be an improvement on the status quo.

3.5

The biggest risk that ATA sees is that under 'voluntary' models, energy retailers will restrict participation in the DRM, limiting the ability to best achieve consumer choice (and the NEO) when compared to a 'non-voluntary' DRM model.

Please refer to the ATA's notes on gaming in 5.1 of this submission.

Without doubt, incumbent energy businesses (that are threatened by the competitive pressure that DRM will bring about), will have a lot to say in response to this question, particularly about claimed gaming risks and implementation costs. In ATA's experience throughout the DRM processes, the debate has been overwhelmed by such claims, most of which are highly questionable (such as the claims that implementation costs will exceed $100M), and some which are plainly spurious (such as the absurd claim that the DRM would result in consumers being paid twice for participation).

Accordingly, ATA suggests that views posited by incumbent businesses in this consultation should be substantiated and explored to ensure they are accurate and balanced, and asks that this question be posed for discussion in a forum with stakeholders that include proponents of the DRM, to ensure some balance in the discussion.

3.6

Yes, a DRM will result in more DR being available to alleviate network constraints and defer network expenditure.

3.7

Currently the scale and behaviour of DR is largely unknown to the broader market, as most of it occurs in off-market arrangements and the remainder that is exercised by or for market customers is done without notification. If an effective DRM were introduced, existing DR customers are likely to participate, improving the demand side information provided.

Question 4 Accredited baseline consumption methodologies

1. In stakeholders' views, are there any alternative demand response mechanism options that would not require the use of baseline consumption methodologies?
2. What might be the costs, benefits, and consequences from having an administrative baseline developed and then managed by AEMO?
3. What are stakeholders' views on the proposed baseline methodologies, and the proposed assessment criteria to be applied when assessing baseline consumption methods?

4.1

No.

4.2

The benefit of AEMO developing a baseline include better independence, consistency and – potentially - efficiency

4.3

The proposed baseline methodologies are appropriate.

Of the proposed assessment criteria, ATA is of the view that "Ease of explanation" is a low priority in this case. The DRM baseline is not something most consumers, even participating consumers, need to understand, any more than other detailed aspects of the NEM. It is entirely inappropriate to compromise other more important criteria in the interest of easier explanation of baseline consumption methods, especially given any 'simpler' method may be less robust in other respects.

Transparency, on the other hand, is a high priority. Accordingly **ATA suggests dropping "Ease of explanation" from the criteria and focussing of the more important aspect of "transparency".**

Question 5 Restrictions on the provision of demand response

1. In stakeholders' views, how effective would the proposed DRM design be in preventing the exercise of potential gaming opportunities?
2. Are there alternative options to improve upon the current design to manage gaming risks?

5.1

Very effective. Many incumbent businesses have raised concerns about gaming of the DRM by participants. AGL, for example, is of the view that DR participants would game the DRM due to

> *'…a strong incentive to inflate the baseline energy consumption.'*
>
> *(Simon Camroux, Business Spectator 12th December 2013)*

In response to AGL's concern, ATA presented a consumer perspective on the incentive for inflating baselines:

> *' [AGL's] concern about gaming demonstrates a lack of understanding of not only the proposed DRM, but of how consumers use energy. The baseline approach proposed by AEMO is similar to that used effectively in other energy markets around the world, with some appropriate customisation for the Australian context.*
>
> *Baseline consumption is calculated on the basis of energy consumed on site over a matter of weeks. Given the intermittent nature of high price events and difficulty projecting them more than hours in advance, to inflate one's long term baseline energy consumption would require energy users to pay much higher bills over weeks and months on the off-chance of the occasional smaller windfall.*
>
> *As a strategy for managing risk and making long term profit, gaming the DRM is up there with playing poker machines."*
>
> *(Craig Memery, Business Spectator 13th December 2013 [3])*

All energy markets carry the risk of gaming, most prevalent in the NEM being the exercise of market power and late rebidding. In ATA's view, the risk that the DRM would be gamed in the NEM is so low as to be trivial.

5.2

None are necessary. Key aspects of AEMO's DRM design include a robust baselining methodology.

[3] http://www.businessspectator.com.au/article/2013/12/13/agl-wrong-demand-response

Question 6 Interactions with demand side participation mechanism

1. Does the proposed DRM design appropriately capture and address all potential interactions between the DRM and other demand side participations options in the NEM?

6.1

There will be opportunities for DRM consumers to provide support for distribution and transmission networks.

Question 7 Prudential requirement

1. Are the proposed prudential requirements on DRAs and retailers appropriate?

7.1

Yes.

Question 8 Settlement charge

1. Do stakeholders have any observations over the proposed changes to the way the costs of ancillary services would be recovered from DRAs and/or retailers?

2. Do stakeholders have any observations regarding the proposed changes to the compensation cost recovery from retailers?

3. Do stakeholders have any observations regarding the proposed changes to the way the operating costs would be recovered from DRAs and/or retailers?

8.1, 8.2 and 8.3

ATA is of the view that these proposed changes are all positive.

Question 9 Implementation issues in relation to the DRM

1. The Council proposes a voluntary approach for retailers to enable their customers to participate in the DRM. How effective do stakeholders think this voluntary approach will be in encouraging retailers to enable their customers to opt-in into the DRM?

2. What are stakeholders' views on allowing manual billing as a viable short term solution to encourage retailers to enable their customers to opt-in the DRM?

Question 10 Voluntary and staged approach

1. The Council proposes a voluntary approach for retailers to enable their customers to participate in the DRM. How effective do stakeholders think this voluntary approach will be in encouraging retailers to enable their customers to opt-in into the DRM?

2. What are stakeholders' views on allowing manual billing as a viable short term solution to encourage retailers to enable their customers to opt-in the DRM?

9.1 and 10.1

To allow any retailer to prevent a consumer from participating in the DRM is simply uncompetitive, undermines the main intention of the Power of Choice reforms: to give consumers choice about demand side participation.

ATA understands the decision by Energy Council to allow retailer's participation to be 'voluntary' is a concession that has been important in reaching accord among COAGEC in progressing the DRM, in the context that retailers expressed concern about the need for system upgrades that relates primarily to the baselining and 'split settlement' of billing/wholesale and network costs.

ATA agrees there is value in implementing the DRM in a way that manages the costs for retailers. As noted previously, this can - and in our view, must - be done without creating barriers to consumers participating in the DRM: 'Voluntary' must not be interpreted to simply give retailers the ability to refuse a customer from participating in a DRM.

As the point of the proposed approach design is to manage implementation and cost for retailers, **what should be voluntary for a retailer is whether or not they are required to modify their settlement and billing systems to accommodate DRM, rather than whether or not a customer participates** per se. If a DRM design can avoid the need for retailers to incur material administration

costs, then there is no justification for any retailer to prevent any customer from participating in the DRM.

Options for the treatment of 'voluntary', that will achieve the goal of minimising or eliminating any the burden on retailers (without the retailer being able to prevent a consumer from participating in the DRM) might include:

- Allowing retailers to undertake manual adjustments rather than implementing automated systems changes (as is the norm for retailers to do when the high cost of changing a system does not justify doing so given the low cost of manual workarounds).
- Simply allowing the retailer to choose whether they separate the wholesale and network charges for a DR customer, as there will be no material impact on the retailer, the market or the network if both of these are settled on the baseline consumption. (In this case, it is possible that complementary arrangements could be made for the customer to recoup any 'overrecovered' NUOS charges directly from the DNSP, in a comparable way to how avoided TOUS is recovered for embedded generators today.)
- Have 'non-voluntary' DRM as the default in the NER and allow individual jurisdictions to make participation 'voluntary' should they choose to do so.
- Move to 'non-voluntary' across the board after a period of, say, 3 years, which will give retailers time to modify their systems their systems to cater to DRM while doing other routine upgrades.

No doubt there are other options available for 'voluntary' participation by retailers that need not restrict consumer participation in the DRM.

9.2 and10.2

Allowing retailers to undertake manual adjustments rather than implementing automated systems changes, as is the norm for retailers to do when the cost of changing a system does not justify doing so given the low cost of manual workarounds, is an effective strategy for ensuring efficient outcomes and should be allowed.

Question 11 Potential barriers to demand side participation in FCAS markets

1. Do stakeholders agree that current market arrangements where only market participants that purchase or sell electricity on the wholesale spot market can participate in FCAS markets are a barrier to entry that restrict DSP in the FCAS markets?

2. Do stakeholders agree that facilitating entry via greater DSP, either as individual or aggregated loads, can result in lower cost and higher quality provision of FCAS services while minimizing the scope to exercising market power in these markets? Do stakeholders have any particular evidence to support their views?

3. In which category ancillary service provision do stakeholders believe that entry will be more likely? Are there any foreseeable future changes that might broaden the scope of entry in markets where demand response has generally not been able to provide ancillary services?

Question 12 Questions on the overall ancillary services unbundling (ASU) proposal

1. In stakeholder's view, how would the ASU proposal impact on the cost of balancing supply and demand in the NEM?

2. Would the ASU proposal result in improved ability for AEMO to manage system security and reliability? What aspect of the rule change would contribute to this?

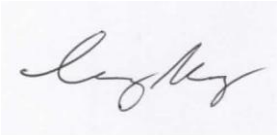
3. Would the ASU proposal result in reduced ability for AEMO to manage system security and reliability? What aspect of the rule change would contribute to this?

Question 13 Interactions with the DRM

1. Does the ASU proposal appropriately capture and address all potential interactions with the proposed DRM?

ATA supports the proposed changes to the arrangements for Ancillary Services.

Thank you again for the opportunity to provide feedback on the Consultation Paper. Please feel free to contact Damien Moyse at damien@ata.org.au with any queries.



Craig Memery
Energy Consumer Advocate
ATA