

Mr John Pierce
Chair, Australian Energy Market Commission
Level 6, 201 Elizabeth Street
Sydney NSW 2000

18 May 2018

Re: EPR0060 – Reliability Frameworks Review - Directions Paper

Dear Mr Pierce

Thank you for the opportunity to comment on the Australian Energy Market Commission's (AEMC) Reliability Frameworks Review Directions Paper (hereafter referred to as the 'Directions Paper').

The Energy Efficiency Council (EEC) welcomes the focus of the Directions Paper on reducing the barriers that are hindering the development of demand response (DR). As we noted in our submission on the AEMC's Interim Report, increased levels of DR in the National Electricity Market (NEM) would significantly increase the affordability and reliability of electricity services.

While the Reliability Frameworks Review self-evidently focusses on reliability, the major benefits of unlocking DR will be increasing competition and reducing the costs of energy supply. Paying consumers to undertake optional DR can:

- Help to maintain the secure operation of the grid through services such as Frequency Control Ancillary Services (FCAS) ("Ancillary Services DR");
- Reduce the need for expenditure on network infrastructure ("Network DR");
- Provide capacity in emergency situations, such as multiple generator failures, at generally much lower cost than either involuntary load-shedding or paying for emergency generators; ("Emergency DR"); and
- Provide low-cost dispatchable capacity in wholesale electricity markets ("Wholesale DR").

Increasing the level of wholesale DR will reduce the need to build and dispatch more expensive forms of capacity and increase competition, placing downward pressure on energy prices. While reforms are necessary to unlock the full potential volume of wholesale DR in the NEM, DR can deliver these benefits whether it is scheduled or price-responsive. We encourage the AEMC to ensure that there are incentives in the market that reflect the benefits of wholesale DR, in order to encourage DR markets and services to evolve.

As we noted in our submission to the AEMC's Interim Report, all the available evidence suggests that the level of DR in the NEM is well below both the economically optimal level and the level seen in overseas markets. To fully unlock the potential level of DR, we need to fully enable and fairly incentivise the value streams from DR.

In Ancillary Services, there has been substantial progress in allowing DR to participate in the FCAS markets. We congratulate the AEMC on implementing the *Ancillary Services Unbundling* rule change in 2017.

In the Network DR category, the Demand Management Incentive Scheme (DMIS) will substantially improve the incentive for network service providers to use DR to reduce expenditure on the network. We look forward to seeing networks using DMIS for this exact purpose.

Finally, in the Emergency DR, AEMO and ARENA's recent RERT procurements demonstrate that hundreds of MW of latent dispatchable DR capability exist in the NEM and can mobilise quickly and at low cost.

While there is more to do in Ancillary Services, Network DR and Emergency DR, recent reforms and off market programs have resulted in fledging growth in DR in all these areas.

However, almost no progress has been made to address the barriers to wholesale DR, with the result that the wholesale market is still dominated by supply-side resources. We believe unlocking the potential for wholesale DR to be a critical priority. In considering how to enable this, we encourage the AEMC to ensure that any reforms that focus on Wholesale DR also create the opportunity for these participants (or intermediaries) to sell these services into all existing and emerging markets for DR services.

The majority of our submission (pages 5-6) focuses on wholesale DR as this is the highest priority for the EEC out of the issues covered in the paper. In wholesale DR, the EEC supports the AEMC investigating Option 1 "*transferring the value of the wholesale demand response from the existing FRMP to the aggregator*", although we recommend that as part of this the AEMC should consider how energy users could directly sell DR into the wholesale energy market.

As we noted in our previous submission, the rapid development of a mechanism to facilitate wholesale DR is essential to rebuild trust in the governance of the NEM. Very little progress has been made to improve demand side participation in the NEM in the 16 years since the Parer Review. We believe that if the rate of reform does not increase, governments and stakeholders will pursue other avenues to reform electricity markets, either through the Energy Security Board or state-based interventions that risk fragmenting the NEM.

The EEC looks forward to continuing to work with the AEMC on its Reliability Frameworks Review. For further information please contact me on rob.murray-leach@eec.org.au or 0414 065 556.

Yours sincerely



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**Energy Efficiency Council submission to the
Reliability Frameworks Review Directions Paper**

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1. Wholesale Demand Response

The EEC welcomes the efforts made by the AEMC to investigate the barriers to DR in wholesale energy markets. The EEC:

- **Reaffirms** our position that the current level of DR in wholesale energy markets is sub-optimal. Facilitating more DR should:
 - o Allow increased transparency and visibility of DR capacity and dispatch;
 - o Enable consumers to have greater choice in their consumption decisions;
 - o Reduce the wholesale electricity price by avoiding the construction and dispatch of more expensive forms of capacity;
 - o Increase competition and thereby reduce the potential for energy market participants to exploit market power for dispatchable capacity; and
 - o Increase the supply of market traded risk management products, putting downward pressure on market prices, and supporting reliability under the proposed National Energy Guarantee (NEG).

- **Supports** the analysis in the Directions Paper that suggests that there are significant practical barriers to wholesale DR. The core barrier is that consumers are required to either be exposed to the spot market price or depend on their retailer offering an attractive DR product. This is problematic, because:
 - o Some retailers may not have or see incentives to offer DR products to customers, and some gentailers could have effective incentives to actively suppress DR;
 - o There is a mismatch in duration between energy retail contracts and DR contracts; and
 - o The lack of competition for demand-response service provision results in many consumers not being offered attractive DR offers.

- **Supports** the AEMC investigating the option of *“transferring the value of the wholesale demand response from the existing FRMP to the aggregator.”* (*The AEMC’s “Option 1”*). This option would partially address the barriers identified above and support the emergence of a competitive market for DR services. While aggregators (including retailers) are likely to be in the best position to unlock the potential for DR, the AEMC should also investigate options that would allow consumers to sell DR services directly into the wholesale energy market – that is, the framework should cater for the possibility that a consumer might prefer to self-manage their own wholesale DR participation, instead of being required to use an intermediary like a retailer or an aggregator.

- **Does not have a position** on the option floated by the AEMC to *“Transferring spot market responsibility for demand responsive load from the existing FRMP to an aggregator”*, but note that Option 1 (above) appears to be more effective than this option.

- **Does not recommend** the option floated by the AEMC to *“[provide] additional incentives for retailers to offer demand response products.”* This proposal would not address any of the barriers noted above, and risks increasing retail margins to the detriment of consumers.

The EEC looks forward to working with the AEMC as it investigates the option of *“transferring the value of the wholesale demand response from the existing FRMP to the aggregator.”* We believe that this option would deliver significant benefits to consumers, both in the emergence of more competitive aggregation services but also a greater range of DR services offered by existing electricity retailers.

The EEC notes that some generators appear likely to oppose any rule changes that would increase the level of DR in the wholesale energy market, as this will reduce their ability to exploit their market power and/or reduce the forward prices of risk management products that they sell today. We continue to be disappointed by the lack of concern that some generators have displayed for both consumer wellbeing and the public good, especially when they are owned by governments.

2. Strategic Reserve

The EEC supports the AEMC’s decision to progress a strategic reserve for emergency situations through two Rule Changes to the Reliability and Emergency Reserve Trader (RERT). We look forward to working through the many detailed issues that need to be considered as part of the two Rule Changes. Based on the discussion and information available to date, our preliminary positions are that the EEC:

- Supports allowing the Australian Energy Market Operator (AEMO) more lead-time to procure capacity under RERT. This will significantly improve the effectiveness and lower the cost of RERT;
- Supports increased transparency and standardisation in RERT contracts; and
- Notes that careful consideration needs to be given on the size of payments for availability (given upfront) and dispatch (only if a resource deploys).

3. Forecasting and Information Provision

The EEC does not have positions at this time on the specific measures canvassed by the AEMC’s Direction Paper on forecasting and information. However, the EEC agrees that more accurate forecasting and information provision will address imperfect information and information asymmetry and encourage more optimal use of demand-side resources.

4. Day-ahead Markets (wholesale energy markets)

The EEC does not have a position on day-ahead markets at this time, and cannot form a position on the suitability of day-ahead markets without more information on proposed models for a market, how it would interact with various aspects of the wholesale electricity market and the impact on energy users and market participants. However, there are a number of points that we can contribute:

Providing energy users with more lead-time to deploy DR will, all else being equal, unlock a greater quantum of DR. While some forms of automated DR can respond rapidly to short-term price signals, other forms of DR require more notice. Some energy users have indicated that the move from 30-minute to 5-minute settlement in the wholesale energy market will result in some energy users reducing their deployment of wholesale DR. We note that this issue is complicated, as the move to 5-minute settlement may provide higher prices for fast-acting DR.

If the wholesale market provides more effective incentives for retailers, aggregators and other parties to encourage DR (see pages 5-6), services are likely to emerge that provide

energy users with sufficient notice and incentives to deploy DR even in the absence of day-ahead markets. For example, if a retailer or aggregator receives the full value of DR deployment and has sufficient information on likely future demand and supply, they could offer energy users a modest price to dispatch DR the day before they are needed. If wholesale prices on the day are at or above the level that is expected then the retailer or aggregator will make a profit, if they are below expected they will make a loss.

The incentive for retailers and aggregators to develop such services depends on a number of factors, including predictability of prices and rewards for dispatching DR. This highlights the importance of addressing other barriers to DR.