



POWERSHOP
A better power company



Meridian.

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12 September 2019

Australian Energy Market Commission
Attention: Mr Declan Kelly
PO Box A2449
Sydney South NSW 1235

Reference: ERCo247

Dear Mr Kelly

Wholesale Demand Response Mechanism, Draft rule determination

Meridian Energy Australia Pty Ltd and Powershop Australia Pty Ltd (MEA Group or Powershop) thanks the Australian Energy Market Commission (AEMC) for the opportunity to provide comments on the AEMC's Wholesale Demand Response Mechanism, draft rule determination (the Determination).

Background on the MEA Group

MEA Group is a vertically integrated generator and retailer focused entirely on renewable generation. We opened our portfolio of generation assets with the Mt Millar Wind Farm in South Australia, followed by the Mt Mercer Wind Farm in Victoria. In early 2018 we acquired the Hume, Burrinjuck and Keepit hydroelectric power stations, further expanding our modes of generation. We have supplemented our asset portfolio by entering into a number of power purchase agreements with other renewable generators, and through this investment in new generation we have continued to support Australia's transition to renewable energy.

Powershop is an innovative retailer committed to providing lower prices for customers and which recognises the benefits to customers in transitioning to a more distributed and renewable-based energy system. Over the last five years, Powershop has introduced a number of significant, innovative and customer-centric initiatives into the Victorian market, including the first mobile app that allows customers to monitor their usage, a peer-to-peer solar trading trial and an extremely successful, large-scale behavioural demand response program.

MEA Group recognises the challenges facing the National Electricity Market (NEM) with the changing mix of generation, retirement of ageing thermal baseload power stations and increase in renewable generation. There is a requirement for innovation in the industry to meet these new challenges. At a high level, incentivising demand reduction at times of system stress can be a useful tool for the market.

However, this should not be the only focus of demand response. Shifting high demand to periods of higher supply should also be a driver of any demand mechanism, which will further support the integration of renewables into the system and assist reducing long term cost of supply.

For a demand response mechanism to be a successful and effective tool it should be capable of being easily and efficiently integrated into the current NEM, market systems and retailing framework with as little disruption as possible.

Costs and benefits of proposed mechanism

The proposed introduction of a new third party NEM participant, the Demand Response Service Provider (DRSP) to aggregate and facilitate demand response between a retailer and a customer, is unlikely to lead to benefits sought by the rule change. There will be limited benefits to the market overall, although individual customers and DRSPs may see some returns over the long term.

These benefits are likely to be offset by increased costs, relating to the new settlement regime, implementation of and supporting new systems, additional DRSP margin and the requirement for retailers to manage the changed risk profile of the remaining portfolio. This will lead to negative impacts on remaining customers. Furthermore, the complexity of the proposed mechanism is likely to increase cost and uncertainty for retailers and customers.

Baselines

A key issue with effective demand response programs is the identification of genuine response, separated from normal or unprompted behaviour. It should be noted that Powershop operates one of the largest demand response programs in the NEM with over 20,000 participants, which is also part of AEMO's Reliability and Emergency Reserve Trader program.

One of the key learnings this program has demonstrated is that it is almost impossible to develop a baseline methodology that rewards genuine participants only. Despite testing numerous baseline methodologies we have been unable to identify a baseline which rewards all genuine participants, all of the time, and not overly rewards non-responsive participants.

The substantial variation of customer usage, behaviour patterns and behind-the-meter generation and storage indicates that it is unlikely that a standardised and centralised approach to baseline methodology will ever be successful. In particular, these variations are likely to increase in complexity over time and will need constant monitoring and readjustment.

To address this difficulty to accurately identify positive responses and the associated complexity of communicating it to customers, Powershop has determined to utilise generous and understandable baselines, so as to ensure that the most genuine participants are rewarded and not discouraged from continued participation. Consequently the business is making a significant investment by rewarding a large number of non-responsive participants, to ensure that the maximum response is elicited and the best short and long term outcomes for the system and our portfolio is achieved.

The Determination would transfer these deemed benefits to the DRSP and other customers, removing any incentive for Powershop, or any retailer that currently runs demand response programs, to continue to make this investment. In addition, there may be a perverse incentive for a DRSP to contract with customers that appear to be responsive under deemed standardised baselines, with no incentive for underlying actual change in consumption or benefit to the market. This will have the consequence of increasing costs for retailers and the overall market.

The key of a long term successful demand response program is the continued engagement of customers and the benefits of educating customers about their usage and the impact on the broader market. Therefore, any baseline that is utilised must ensure that customers are encouraged to respond in ways that actually assist them and the market over the long term.

Reimbursement rate

As noted above, MEA Group believes the reimbursement rate should not only cover the cost incurred in hedging for demand response customers, but also consider the overall impact on a retailer's portfolio. The reimbursement rate proposed does not reflect the actual cost of supplying and hedging an individual customer's load. As the reimbursement rate is based on the net system load shape, it will excessively penalise retailers with a portfolio of peakier customers. As DRSPs are likely to target customers with a higher demand at times of peak prices, it is likely that the Determination will over-compensate DRSPs and under-compensate retailers.

Powershop anticipates most retailers will respond rationally to this economic incentive to actively avoiding demand response customers due to higher costs of supplying and increased uncertainties. The net result may be that neither the market nor the individual participating demand response customers will receive the expected long term benefits of the Determination.

System changes

MEA Group believes the Determination will lead to significant development of, and modifications to, additional systems, processes and employee costs on implementation of the new mechanism and to monitor on an ongoing basis.

While it is always difficult to estimate such costs in advance, especially with the Determination still in draft form, our experience with other similar regulatory changes is that these costs, timeframes and implications can be very significant.

This includes not only costs, but also the displacement of other desirable system changes and developments which may have greater customer and market benefits. Recent regulatory changes, including Power of Choice, 5 Minute Settlements, Default Market Offer, Retailer Reliability Obligation etc. have resulted in Powershop either deferring or cancelling significant planned upgrades, initiatives and innovations which we believe would have had delivered significant customer benefits.

MEA Group is strongly supportive of the role of demand response and will continue to develop and explore opportunities in this area with our customers and partners. These will ensure that the value created is shared with customers and benefit the market as a whole. We encourage the AEMC to continue to identify means of ensuring that demand response is promoted and utilised to the maximum extent feasible, without undermining existing desirable market outcomes. We are not convinced that the proposed complex mechanism and the creation of separate market participants will achieve this outcome.

If you have any queries or would like to discuss any aspect of this submission please do not hesitate to contact me.

Yours sincerely,



Michael Benveniste
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Meridian Energy Australia