



PO Box 4136
East Richmond VIC 3121
T 131 806
F 1300 661 086
W redenergy.com.au

PO Box 4136
East Richmond VIC 3121
T 1300 115 866
F 1300 136 891
W lumoenery.com.au



16 February 2023

Ms Jessica Curtis
Project Lead
Australian Energy Market Commission
GPO Box 2603
Sydney NSW 2000

Submitted electronically: aemc@aemc.gov.au

Dear Ms Curtis,

Re: ERC0346 consultation paper - Unlocking CER benefits through flexible trading

Red Energy and Lumo Energy (Red and Lumo) are pleased to make this submission to the Australian Energy Market Commission's (the Commission's) consultation paper on a rule change proposal by AEMO relating to the benefits of Consumer Energy Resources (CER).

We do not support AEMO's rule change proposal or any other measure to allow for multiple providers of competitive retail services at a customer connection point. A variation of this proposal was assessed as part of the Power of Choice reforms and the same operational problems identified then remain, while the same questions about whether it would generate a net benefit for consumers remain. Moreover, the perceived problem that AEMO is trying to solve no longer exists.

There are no obstacles at present to active demand side participation or the provision of network and system support, whether in direct response to price signals or through distributed generation. The competitive market already delivers effective solutions for consumers who can have control over the timing and volume of their consumption. Larger consumers are the main beneficiary today, but nothing stops smaller consumers participants other than their cost/benefit trade off.

Combined with ongoing technological advances and further reductions in the cost of CER, the market is also starting to deliver similar solutions for smaller consumers on an increasing scale. Until the recent AEMO Virtual Power Plant (VPP) demonstrations, small customer CER aggregators were not able to offer Frequency Control Ancillary Services. Contestable market providers are offering VPP customers a share of the proceedings of participation in this market now that this material component of the CER value stack is accessible.

The AEMO flexible trading proposal differs from such initiatives because it will dilute value and generate substantial costs, rather than offering a new source of value.

Current levels of CER utilisation

We see no compelling evidence that there is a significant market failure that warrants a change to the current framework or that the current level of demand side participation is deficient, particularly where the proposed change has such high potential for disruption. There are significant risks that policymakers and regulators will try to encourage CER uptake—particularly by smaller consumers—by changing the fundamental design of the NEM and creating distinctions between competing entities, and also by unwinding core protections and established standards and procedures. If anything, the proposed changes will undermine the competitive market and ultimately stymie the development of retail service offerings that offer load flexibility.

The Commission points to estimates of the potential benefits of more active CER participation as a reason to consider rule changes; an example is the Australian Renewable Energy Agency's *Valuing Load Flexibility in the NEM* study.¹ However, we recommend caution when comparing the tangible and significant risks of the proposal against the frequently cited estimates of benefits. These estimates are highly dependent on assumptions about the volume of CER across the economy and the firmness of consumers' responses to sharper price signals. More significantly, they do not rely on fundamental changes to market structure in the form that AEMO proposes.

At this point in the energy transformation, there may be limited appetite among smaller consumers for large scale active participation, even among those with CER. Indeed, many of these consumers look to their retailer to limit price risk rather than face sharper price signals. Further limitations are some of the obstacles to behavioural change that the Commission refers to in the consultation paper and which the Energy Security Board is analysing in its Customer Insights Collaboration.

Few smaller consumers appear willing to relinquish control over their CER and substantially alter their consumption. For example, the majority of owners of electric vehicles (EVs) consider their asset to be a mode of transport rather than as a battery on wheels, and most consumers are reluctant to relinquish control over important appliances, such as airconditioners. These consumers are making a perfectly rational decision, valuing the electricity they consume more than going without.

A further issue for the Commission to consider when assessing whether the level of CER participation is deficient is that many examples to this point have occurred through subsidised

¹ Australian Renewable Energy Agency (2022), *Valuing Load Flexibility in the NEM*

trials involving commercial and non commercial entities, such as ARENA and the CSIRO. These trials provide valuable insights but it is possible they have crowded out commercial initiatives in recent years. The Commission should bear this in mind when assessing the current level and form of CER takeup, and whether the competitive market is capable of delivering efficient outcomes under the current regulatory framework.

It is vital that the Commission recognise that these are not examples of market failure or regulatory obstacles. Competition is increasingly encouraging retailers to continue to identify consumers across all segments who are interested in more active demand side participation.

Recommended approach

Red and Lumo encourage the Commission to take a broad view of the evolution of CER across the NEM and the drivers of its further take up in the near future. We see no need to proceed with the AEMO proposal. This aspect of the market may be in its early stages for small consumers but it is likely to grow substantially in coming years. Furthermore, effective competition provides a strong incentive for retailers to offer retail products that reflect consumers' willingness to participate in the market through CER (or not); otherwise they will lose market share. This will evolve and develop organically in response to consumer demand. We would welcome the opportunity to follow up this submission with a meeting with the Commission to discuss how we see the market developing, including to discuss some of our initiatives.

The Commission should also consider how national initiatives will align with jurisdictional schemes relating to CER, and to emphasise the importance of consistency. For example, the Energy Security Board is considering how to account for EVs in the energy transformation, while state governments continue to develop their own policy initiatives. We are hopeful this will produce investment certainty for CER. Competitive retailers are already developing offerings tailored to EV owners and policy certainty—in terms of network pricing and charging infrastructure, for example—would accelerate this.

The remainder of this submission discusses our main concerns with the rule change proposal in more detail. They are as follows:

- Greater volatility of retail load, particularly for currently authorised retailers. This will add to hedging costs and undermine retail competition.
- Costs of implementation and ongoing operations, both for the primary Financially Responsible Market Participant (FRMP) and any other competitive entities at a site.

- Potential to jeopardise competitive neutrality, noting the need to allocate network costs, exposure to credit support obligations and consumer protection obligations between competing entities.
- Potential for poor customer experience, noting they will need to deal with multiple service providers and there is potential for confusion and misunderstanding, particularly in the event of disputes between customer and service provider.

Implications for retail load and subsequent impact competition

The consultation paper acknowledges the impact on the primary FRMP of allowing for competition at a consumer's connection point. It describes the potential hollowing out of load and for consumers to pursue arbitrage opportunities. For example, the Commission describes a scenario where a consumer could switch resources between settlement points, consuming electricity on spot prices when wholesale prices are low and exporting at the other connection point on a fixed price, and then reversing that arrangement when spot prices are high. However, this underplays the impact of the greater exposure of the primary FRMP to volatile and unpredictable load behind the secondary meter. While it appears that the consumer *could* benefit from this, the increased costs will significantly offset any potential benefit.

A further contributor to the volatility and unpredictability of retail load is that the consumption or output from assets that are operating behind secondary meter points may be dependent on less reliable infrastructure and communications networks. This means they could be prone to frequent dormancy without notice. An example might be a residential wi-fi network. FRMP1 also has no visibility of the commercial arrangement between the consumer and any other commercial entity. The latter may choose to end the arrangement, disconnect a CER asset or take other actions to avoid exposure to non payment risk that influence the volume of energy that FRMP1 is liable for.

This consequence of the rule change proposal and the impact on the primary FRMP (or FRMP1)—who remains responsible for wholesale settlement with associated prudential requirements, and for network costs—is one of the main problems we see with this proposal. We are not confident that this is easily managed through some of the mechanisms that AEMO proposes. These include allocating responsibility for managing settlements and network costs to the FRMP1, relying on accreditation and operation of metering data provision and Metrology Procedures requirements for validation and substitution of data to manage grid isolation, and deactivation of secondary settlement points in MSATS as an alternative to de-energisation. These will take some time to develop and even then will be imperfect solutions. They will either add further to the cost of serving that consumer or fail to achieve an appropriate allocation of risk between competing entities.

Predicting and then managing retail load becomes very challenging for conventional retail operations under these circumstances. This will add to hedging costs and flow through to retail offers in some way, which could be through an increase or change in structure to reduce exposure to more variable consumption and output patterns. Other retailers may scale back their operations or leave the market completely, reducing competition and undermining innovation. In these circumstances, the net benefit to consumers of this change to market structure is highly uncertain.

The consultation paper states the following:

'... where CER aggregators are able to generate value from trading CER in the wholesale market under the current framework, they have to share that value with the existing retailers instead of being able to share this value directly with consumers. Small margins may not result in deals at all and existing retailers may add a margin before sharing cost reductions with the customer. This would mean customers face the risk of receiving less value from their CER being traded in the market than if they could directly engage with CER aggregators to trade their flexible resources in the markets'.²

It is highly questionable whether the aggregator is adding an additional service in this situation. Rather, it is simply diluting the same value while adding to cost to serve (CTS). A retailer is equally able to participate in the market in this way and share the benefits with their customer; this is a common feature of retail contracts with customers (generally with large, flexible load) at present.

More generally, a FRMP who has complete understanding of their customer's site, assets, historic consumption profile, circumstances and preferences will offer a more complete service that optimises consumption and the utilisation of different types of CER and shares those benefits. A participant who only provides a narrower service will not be able to do this.

Costs of implementation and ongoing management

A change to market structure on this scale, involving new participants and rules and procedures, will be very costly to implement for participants and for AEMO. We note AEMO's current consultation on the proposed *Participant Fee Structure for the NEM 2025 Reform Program*, which estimates total program costs of \$430m to \$600m (with a +/- 40% level of accuracy); Integration of DER and Flexible Demand is one of the main pathways in this program.³

² Australian Energy Market Commission (2022), *Unlocking CER benefits through flexible trading, Consultation paper*, page 15

³ AEMO (2023), *Structure of Participant Fees for AEMO's NEM 2025 Reform Program*

This coincides with a period of elevated wholesale pricing and the Australian Energy Regulator's objective to reduce retailers' CTS as part of its vulnerability strategy.⁴ On implementation costs, the Commission could obtain details from AEMO and market participants of the cost of implementing the Power of Choice initiatives as part of its assessment of the cost of implementing the AEMO flexible trading proposal.

We are also concerned about the incremental contribution to CTS and therefore, the impact on consumers. These include the additional costs for FRMP1 and for any additional market participants. Each new participant operating at the site will incur initial set up costs and CTS, while also expecting a reasonable return on that outlay.

We note AEMO's suggestion to reduce metering costs through reduced requirements and specifications for meters at secondary settlement points.⁵ However, the difference in amortised capital costs between the two meter types is likely to be very small, even when some costs are stripped out through a reduction in specifications. Furthermore, this will not reduce initial installation costs and any ongoing costs to maintain the meter.

As proposed, AEMO's rule change would impose additional costs on FRMP1, potentially placing it at a competitive disadvantage relative to direct competitors. This includes the coordination of settlement and network costs (including demand tariffs, credits and any future export charges) over and above any change in risk profile this creates.⁶ FRMP1 will be responsible for complying with prudential requirements and must comply with network credit support obligations. As mentioned in the previous section, it will be very difficult to develop rules and procedures that efficiently allocate costs and risks between competing parties.

Competitive neutrality

We see high potential for the proposal to undermine competitive neutrality and therefore effective retail competition over the longer term. This would be to the detriment of consumers across all segments. This issue is broader than the differential impact on CTS discussed in the previous section. AEMO proposes different regulatory and procedural obligations for competing market participants, whether this is through alternative arrangements for meter providers at secondary settlement points or the minimum terms and conditions between consumers and FRMP1 and its retail competitors who are installing secondary meters.

⁴ We note a recent open letter from the AER to stakeholders regarding its review to simplify the retail market regulatory framework, available at www.aer.gov.au/retail-markets/guidelines-reviews

⁵ It is unclear how the Consumer Data Right will account for data from 'minor energy flow meters'; this may require changes to the current designation instrument

⁶ A further issue is that the proposal could undermine the objectives of network tariff reform by inhibiting the price signals that distribution network service providers are seeking to provide to end consumers.

The Commission is aware of the Australian Energy Regulator's review of consumer protections for future energy services, which is directly relevant for this review. We repeat the position in our submissions to that review that the starting point for the regulation of energy, including any new services, is to acknowledge its status as an essential service. As a consequence, any entity involved in the sale or supply of energy, including the ability to interrupt that supply, must comply with the same core consumer protection obligations.

These include obligations to notify of prescribed events and changes to key terms and conditions, strict controls over disconnection and interruptions to supply, and complaint resolution obligations (such as access to ombudsman schemes). These obligations create compliance costs while also limiting a market participant's ability to manage their exposure to bad debt. The Commission is aware of other obligations that apply to the sale of energy outside the National Energy Customer Framework, such as the Default Market Offer Code and the calculation of concessions. It will be very difficult for FRMP1 to comply with these latter obligations when there are multiple settlement points and we do not see an easy solution to allocating them between competing entities.

Any framework that does not allocate regulatory obligations appropriately between competing entities will undermine competition by favouring particular business models. Moreover, it would reflect an implicit assumption that core protections should apply to the consumption of energy in some situations but not to others. The National Energy Customer Framework was never designed in this way and core protections have been extended to apply to sellers of energy other than authorised retailers, i.e. exempt sellers, in recent years, rather than scaled back.

The notion of applying different regulatory obligations to different energy market participants is a confusing message for consumers. Furthermore, a more complex regulatory framework creates significant problems for regulatory oversight and administration.

Customer experience

As noted, consumers would need to understand what protections apply to particular circumstances and it will not always be obvious why some apply in some instances but not others. This includes avenues for recourse in the event of a dispute or advance notification of an interruption to or disconnection of supply.

More generally, consumers will have the choice to engage with multiple service providers but we see high potential for confusion, duplication and misunderstanding when the frequency and form of information and communications they receive will probably differ but the underlying service, i.e. the sale or supply of energy, is broadly the same.

About Red and Lumo

We are 100% Australian owned subsidiaries of Snowy Hydro Limited. Collectively, we retail gas and electricity in New South Wales, Queensland, South Australia, Victoria and in the ACT to over 1.2 million customers.

We thank the Commission for the opportunity to comment on its consultation paper. Should you wish to discuss aspects of this submission or have any further enquiries, please contact Sean Jennings on 0403 846 585 or me on 0438 671 750.

Yours sincerely

A handwritten signature in black ink, appearing to read "G Hargreaves".

Geoff Hargreaves
Manager - Regulatory Affairs
Red Energy Pty Ltd
Lumo Energy (Australia) Pty Ltd