



16 February 2023

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

Dear Ms Curtis

## **RE: Flexible Trading Arrangements**

Shell Energy Australia Pty Ltd (Shell Energy) welcomes the opportunity to respond to the Australian Energy Market Commission's (AEMC) consultation paper on unlocking consumer energy resources (CER) benefits through flexible trading arrangements (FTA).

## **About Shell Energy in Australia**

Shell Energy is Shell's renewables and energy solutions business in Australia, helping its customers to decarbonise and reduce their environmental footprint.

Shell Energy delivers business energy solutions and innovation across a portfolio of electricity, gas, environmental products and energy productivity for commercial and industrial customers, while our residential energy retailing business Powershop, acquired in 2022, serves more than 185,000 households and small business customers in Australia.

As the second largest electricity provider to commercial and industrial businesses in Australia<sup>1</sup>, Shell Energy offers integrated solutions and market-leading<sup>2</sup> customer satisfaction, built on industry expertise and personalised relationships. The company's generation assets include 662 megawatts of gas-fired peaking power stations in Western Australia and Queensland, supporting the transition to renewables, and the 120 megawatt Gangarri solar energy development in Queensland.

Shell Energy Australia Pty Ltd and its subsidiaries trade as Shell Energy, while Powershop Australia Pty Ltd trades as Powershop. Further information about Shell Energy and our operations can be found on our website [here](#).

## **General Comments**

Shell Energy does not support the introduction of FTA in the National Electricity Market (NEM). In the seven years since the AEMC considered this issue through the Multiple Trading Relationships (MTR) rule change, we do not see that enough has changed to warrant the rule change being made. Based on the rule change request, we have identified several key areas that demonstrate that FTA is unnecessary and inefficient. These include:

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<sup>1</sup>By load, based on Shell Energy analysis of publicly available data.

<sup>2</sup> Utility Market Intelligence (UMI) survey of large commercial and industrial electricity customers of major electricity retailers, including ERM Power (now known as Shell Energy) by independent research company NTF Group in 2011-2021.

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- There are already multiple ways customers can receive the benefits FTA are slated to bring, without the need for the rule change;
- the costs and risks of the proposed rule change will far outweigh the potential benefits that may arise for a small subset of consumers;
- imposing all network charges on the primary financially responsible market participant (FRMP) may not be compatible with consumer protections such as the Default Market Offer (DMO) and Victorian Default Offer (VDO) and may lead to increased overall costs to consumers, confusion and misleading offers that make retailer comparisons difficult;
- decision-making based on the incentives of individual, disaggregated loads risks making customers worse off overall and not truly optimising the benefits of their CER;
- the impact on vulnerable customers such as customers with life support or on hardship programs has not been adequately addressed; and,
- the presence of multiple retailers at the one site increases complexity and confusion for customers and the risk of billing disputes and ombudsman cases.

Traditional electricity retail businesses rely on economies of scale. Because of the significant costs of establishing systems and processes to meet market and regulatory requirements, in addition to meeting prudential and credit support requirements, retailers seek to maximise the volume of electricity that is sold to (or purchased from) customers to access a stronger return on investment. This is also why large electricity users can generally access lower electricity rates than small users.

While the market is certainly in period of transition where more consumers can generate, store and actively control their demand, this will not change the fundamental reality that contracting for a greater volume of electricity for a customer would be preferable to a lower volume. In contrast, the rule change request assumes that a retailer would choose to offer to sell or purchase a portion of a customer's load, rather than servicing their entire load. The only reason we can imagine that a retailer would make such an offer is if its strategy was to acquire small volumes from customers that it otherwise would not be able to win (i.e., a small volume is better than no volume from that customer).

However, if the retailer is unable to make an offer that is sufficiently competitive with the incumbent offer for the entire load, it is unclear how reducing the volume would allow it to offer a more competitive offer. This would be contrary to the basic economies of scale on which retail businesses are built. The only way that this could be achieved is by imposing fewer regulatory obligations on the secondary trader or offering a product that places all market risks on the primary FRMP (e.g., offering a pool-price pass through arrangement where consumption automatically switches to the primary FRMP when prices exceed an assumed retail rate). These options would not be in the best interests of the market as a whole, as they would distort the retail market and may even increase risks to system reliability and security.

It is also important to note that customers with FTA-arrangements would be more costly to serve given the increased risks to hedging and energy forecasting in particular. The operational costs we expect retailers to incur are only likely to increase with customer uptake. All retailers would face the risk that an existing customer could take-up an FTA arrangement with another retailer, and therefore could not avoid the costs associated with supporting such customers. These risks could be heightened at times of high market prices or during RRO periods for instance.

All told, Shell Energy considers the proposed rule change as unnecessary. The proposed rule change would impose significant costs and there are already opportunities available to consumers that allow them to find separate value for CER. As such, to the extent that any changes are needed, we recommend this focus on actions such as developing new methodologies for the Wholesale Demand Response Mechanism (WDRM).



### **Optimising and obtaining value from CER for consumers**

CER offer consumers separate value streams that can balance against their consumption. The rule change proposal appears to suggest that consumers, if they so choose, should be able to unbundle parts of their consumption and generation to maximise the value they can receive. A retailer that does not offer a competitive offer for one of these streams could be replaced by another so that the consumer can maximise the value their resources provide.

We note that in disaggregating their load and generation, it could significantly add complexity to a consumer's interaction with the retail market. While certain consumers may be comfortable engaging multiple FRMPs and managing the relationship, we maintain that the vast majority of consumers would prefer a simpler arrangement, with one retailer handling all aspects of their electricity consumption and generation. We consider the AEMC must balance the potential value for some consumers against the added complexity and confusion that this could bring to the retail market.

In addition, Shell Energy's experience as a provider of energy solutions to both retail and non-retail customers has taught us that there is a distinct risk that engaging multiple providers at a site could in fact reduce opportunities for customers to optimise CER. A single FRMP at a site would be able to engage in a range of bespoke activities to reduce both energy costs, network tariffs and potentially taking advantage of spot prices for export such as by load-shifting, peak-shaving, charging and discharging batteries at certain times etc. In contrast, a secondary retailer which is not exposed to the network tariff or has no visibility of the rest of a customer's load is likely to only undertake actions which make economic sense for them as a retailer absent the rest of a consumer's demand. For instance, a retailer focussing solely on the spot price may choose not to dispatch a battery or turn down HVAC systems during a critical peak day for network tariffs if the spot price is not high enough. A FRMP with visibility of the whole site may act differently because when looking at a customer's entire demand and economic picture, the customer could benefit from reducing demand even in the absence of high spot prices. The reverse is also true, a secondary trader could actually increase demand through charging a battery in anticipation of high wholesale prices at a time when the optimal response could be to not consume because of network tariffs. To summarise, this rule change risks creating an environment where decision-making based on the incentives of individual, disaggregated loads results in customers being worse off overall.

In some instances, consumers may be able to benefit from separate arrangements for their CER. This is why some large consumers may contract separately their large and small sites. However, consumer have options now that do not require the introduction of flexible trading as described in the rule change request. The Small Generation Aggregator (SGA) framework, and the WDRM represent two significant opportunities for consumers. We do note that small consumers are currently not able to participate in the WDRM. This would be better addressed through changes to existing structures such as the WDRM or through retail tariff reform than a more costly and risky proposal in the form of the FTA rule change.

### **Existing and future CER products and services**

The AEMC asks whether the introduction of flexible trading could create an environment that fosters the development of more innovative products and services to support consumers to optimise and obtain value from their CER.

In response, Shell Energy argues that existing opportunities available to consumers, and the prospect of future opportunities arising demonstrates the FTA rule change is unnecessary. There are a range of mechanisms that currently allow consumers to engage multiple providers without the need for additional regulatory reform.

Shell Energy has developed a LoadFlex product which allows us to control and optimise the use of CER – including demand response, battery storage, solar PV and EV charging – to deliver benefits across a whole site



to customers regardless of whether we are the FRMP or not. Our approach leverages the SGA framework and achieves the same purported benefits that FTA will bring without the need for any further regulatory change.

Our approach to leveraging multiple CER for multiple benefit streams (energy market, DNSP support services and customer savings) is to co-optimize the performance of these resources at the point of connection. Where we are not the FRMP, we use the WDRM for all CER excluding batteries. For batteries, we use the SGA framework at the site.

As part of this approach, we are currently working on an Australian Renewable Energy Agency (ARENA) program to commercialise the full integrated CER solution for commercial & industrial customers called Smart Energy Hubs.<sup>3</sup> Milestone 1 for this project is at the end of February 2023 and will include significant information on the learnings from initial projects and the intended strategy for unlocking regulatory reforms and DNSP support services.

In the case of electric vehicles (EV) a technology regularly cited as standing to benefit from FTA, with a secondary leasing company handling EV charging only rather than a customer's entire load. In our experience, changes to regulatory framework should not be necessary for this to occur. Shell Recharge Solutions operates a model in the EU that allows customers of any retailer to have their EV charging costs billed to the fleet owner.

In addition, there are opportunities for customers to participate in Virtual Power Plants (VPPs) using their batteries or solar PV now.

With all these options in the market now, Shell Energy considers that the introduction of FTA is not needed for consumers to optimize the value of their CER.

### **Competition issues with secondary settlement points**

Taking the entire perspective of the rule change into consideration, Shell Energy contends that the FTA rule change is likely to negatively impact competition. We accept that making it easier for other parties to compete to supply electricity to consumers could provide competition benefits. This only holds true if the parties are competing on a level playing field. As is made clear in the AEMC's description of the rule change, it is unlikely that parties would be competing on an even basis. As such, Shell Energy considers the rule change is likely to detract from competition. This is due to the advantages seemingly given to the secondary FRMP(s) such as:

- not bearing the credit risk for network tariffs;
- being able to price customers without including network tariffs;
- potentially being able to shift load at times of high prices back to the primary FRMP; and,
- uncertainty whether the same regulatory requirements apply, e.g., hardship, family violence, life support, best offer notification, price regulation (e.g. VDO or DMO). This will add complexity and put customers at risk.

As an initial point, we strongly dispute the Australian Energy Market Operator's (AEMO) assertion that the rule change will "...not impose material costs on participants other than those that wish to provide [FTA] services..."<sup>4</sup> The proposed rule change will create a need for all retailers to adjust systems to cater for the prospect that some consumer load can be shifted to a secondary trader – and potentially shifted back – at will. This undermines existing billing, trading, pricing, forecasting and settlement systems. All will require some level of change to cater to this rule change if it is made. Without a more concrete proposal, it is difficult to provide a

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<sup>3</sup> Shell Energy Smart Energy Hubs Deployment Project

<sup>4</sup> AEMO, Electricity Rule Change Proposal: Flexible trading arrangements and metering of minor energy flows in the NEM, May 2022, p18.



reasonable cost estimate. There is too much variance that depends on particular design choices. However, the fact that the model proposed under the rule change request would impact systems relating to the entire lifecycle of a customer means that the costs are likely to be significant if that approach is implemented.

We also consider that there are major risks from allowing electrical connections to be able to switch consumption from one FRMP to another, potentially at will. While there may be potential benefits to individual customers, it imposes an unacceptable level of risk on the primary FRMP, particularly during high-priced events or during an RRO gap period. This risk was part of the driver in the RRO opt-out provisions contained in Clause 4A.D.4(5) of the National Electricity Rules (NER), to require an opt-in customer to opt-in for all connection points at a site. In simpler terms, load which is more volatile or 'peaky' is more costly to hedge and as such is more costly to serve. This is likely to translate into higher prices for consumers.

We strongly oppose any design option that would allow users to move consumption from one FRMP to another at will. It imposes financial and risks well above and beyond those of regular consumption variability, particularly at times of high prices.

For example, during the high-priced market events in May and June 2022, secondary retailers could have simply switched consumption back to the primary FRMP as prices remained high, therefore placing the financial risk back to the primary FRMP. During an RRO gap period, secondary retailers could switch consumer load back to the primary FRMP during the relevant times, absolving or severely limiting their own RRO liability while increasing the risk of non-compliance to the primary FRMP.

The allocation of network costs also creates a potential impact on competition. We will provide a more comprehensive assessment of the proposed approach to network tariffs later in this submission. With respect to its interaction with competition, and in particular price regulation such as the VDO and DMO, the fact that a secondary FRMP would not need to include network tariffs in offering tariffs to consumers means that the tariffs offered by secondary traders will be artificially lower than those a primary FRMP is able to offer. Not only is this an unreasonable competitive disadvantage for the primary FRMP but there are feedback loops which could result in consumers being worse off. If secondary FRMPs face lower consumer protection obligations, these will be enhanced further. Take for example, a simple situation where a consumer's primary FRMP makes the following offer to a small customer in Victoria, with an assumed annual consumption of 4000 kWh:

- Daily supply charge: \$1.00
- Electricity Tariff: \$0.24/kWh

Using data from the AEMC residential Electricity Price trend report, the assumed split of costs is \$0.08/kWh for wholesale costs and \$0.12c/kWh for network charges, with the remainder being made up of environmental costs and a residual (margin and retailer costs).

Assuming FTA is introduced, a secondary FRMP then enters the market to offer customers a portion of their load (in this example 500kWh) to be supplied at \$0.15/kWh. A customer may see this as an attractive proposition as the secondary FRMP is offering energy significant cheaper than their primary FRMP. This is only because network costs will be paid by the primary FRMP. If we add the network costs, then the consumer would actually be paying \$0.27/kWh, a more expensive tariff than the primary FRMP offers.

Under FTA the primary FRMP is then likely to change their electricity prices to factor in the network costs they are still required to pay. If this increases the headline tariff that the primary FRMP can offer consumers, then it would widen the gap between what they are offering and what a secondary FRMP can offer, making offers from secondary retailers appear more attractive. However, the secondary FRMP is only able to offer 'cheaper' rates because it does not include a significant proportion of the cost base and therefore masks the true financial impact. Unbundling network charges from bills would increase transparency but would create operational costs for energy retailers and increase complexity on bills.



Introducing these dynamics will also make it more difficult for small customers to compare retail offers, adding complexity and risk. Further, it is unclear how 'best offer' provisions would apply to customers with multiple FRMPs at a site.

We also query how this would function in terms of the Default Market Offer (DMO) or Victorian Default Offer (VDO). The DMO or VDO represents both a reference price and an effective price cap on small customer energy costs. If a customer is entitled to the DMO price for all energy consumed via the primary FRMP, but the primary FRMP must also charge for all network charges, a mismatch arises. The primary FRMP would then be required to price a customer based on network consumption at one volume and energy consumption at another. This risk is heightened for higher consumption devices that may be utilised under FTA such as electric vehicles (EV). The lower the proportion of a customer's total load the primary FRMP bills for, it may be harder to develop tariffs that meet the requirements of the DMO or VDO.

### **Allocating network costs**

As the rule change proponent, the Australian Energy Market Operator (AEMO) proposes to levy all network tariffs on the primary FRMP. In our view, this area is one of the major challenges of this rule change. In effect it would mean that the primary FRMP would bill a customer for all network tariffs alongside a subset of consumption. AEMO argues that the competitive retail market should be able to adjust to this complexity. As discussed above, this approach could create a competitive advantage for retailers at secondary connection points that do not need to charge for network tariffs.

AEMO's view that the competitive retail market should be able to adjust also misses several important points. Large customers are more frequently billed with unbundled tariffs. For example, Shell Energy bills its customers with network tariffs as a separate line item. AEMO's preferred approach would then mean that we would bill customers for differing network consumption and energy consumption amounts. This approach would create the need for system changes as our billing system is designed for the figures to match. As such, FTA will impose costs on us, regardless of whether we intend to offer FTA services or not.

In the case of small customers, moving to a situation where energy and network charges are unbundled would run counter to the desire to simplify customer bills through the AER's Better Billing Guidelines for instance.

The bigger issue is the risk of customer complaints and increasing cases to ombudsman services as consumers may not fully understand the implications of any FTA arrangements they have entered into. Even increased inquiries place a burden on examining cases to find the root cause of customer queries. Based on our experience, we already receive inquiries related to customers who have SGA arrangements with a different party. Shell Energy therefore considers that although allocating network tariffs solely to the primary FRMP may be the simplest approach for AEMO and networks, there are risks that are not easily resolved.

In addition, the preferred approach would leave the primary retailer bearing the credit risk of bad debt and working capital for network tariffs. This creates an uneven playing field which advantages secondary traders. Currently, retailers pay network bills to TNSPs and DNSPs before receiving payments from customers. Retailers therefore bear the costs when customers do not pay. Under FTA, secondary FRMPs would only face the credit risk for the energy component of bills if customers do not pay.

The alternative options are also not without risk or costs. Requiring DNSPs to develop separate tariffs to be shared between FRMPs will impose a cost of DNSPs required to develop them and adjust internal systems to cater to these new arrangements, the costs of which would be passed onto consumers. This applies equally to having a third party perform a 'wash-up' service. A hybrid system applying for secondary settlement points exceeding a certain limit would impose costs on DNSPs as well as creating a risk of gaming as traders may seek to consume less than any pre-determined capacity limit. Requiring the FRMP at the primary connection point to pass on charges and credits imposes an additional burden. The primary retailer would have to bill multiple





FRMPs, while not entirely resolving the credit risk issue; presumably the primary FRMP would still have to pay the DNSP in advance of receiving funds back from secondary retailers.

Shell Energy considers that all network cost options have drawbacks. Levying all network charges on the primary FRMP may be the simplest option, but it distorts the retail market. If anything, we contend that this issue highlights a fundamental flaw in the overall FTA proposal and has been largely overlooked in the rule change request.

### **Potential for limitations applied at secondary settlement points**

The rule change request proposes that the NER be amended to establish specific exclusions, with the FRMP for a secondary settlement point responsible for complying with those restrictions. These restrictions could be related to the capacity of the electrical equipment, the nature of resources (e.g. excluding life support equipment) or a combination.

Shell Energy considers the need for restrictions highlights yet another challenge with this rule change. Electricity is an essential service and is regulated as such. Carving out certain kinds of supply for exclusion changes the nature of electricity as an essential service. It suggests that some proportion of electricity consumption is essential while another is not. At some level this is true: watching TV is far different from life support equipment for instance. But how essential the supply is changes with context. Air conditioning or heating may not be essential on a mild spring day but may be essential during a cold snap in winter or a heatwave in summer.

A capacity limitation could also prevent the primary retailer's load being hollowed out, with the FRMP bearing responsibility for all network tariffs and a very small proportion of load. This would limit some risks to the primary FRMP. Yet, if a consumer were consuming a high proportion of their load via a secondary FRMP, then surely the secondary FRMP should bear the responsibilities and obligations that come with being the primary FRMP.

Shell Energy agrees with the need to specifically exclude some devices like life support equipment from being subject to FTA arrangements. However, the fact that such moves would be required highlights the risks involved in this rule change. There is a range of equipment that can be classified as life support equipment such as hot water, medically required heating and air conditioning which make it challenging to establish exclusions. This difficulty is exacerbated if a life support customer moves into a premises that is already set up for FTA with multiple FRMPs. It is therefore hard to see how the benefits of making this rule change could outweigh the risks involved when it comes to major consumer protections like life support.

### **Consumer protections**

The issue of consumer protections is an important one in the context of this rule change. The AEMC has correctly identified issues such as price regulation (DMO or VDO), life support, family violence, hardship, move-in and move-out arrangements, and re-energisation.

To add to this, Shell Energy is concerned that the proposal risks adding complexity and confusion back into the retail market. Reducing the level of confusion in the retail market has been a core drive of regulation such as the Default Market Offer (DMO), Better Bills changes and best offer notification. Adding complexity through multiple connections and FRMPs at a single site could undo much of the significant investment in systems and process changes to support these initiatives.

Shell Energy is surprised that the issue of consumer protections has largely been passed onto the AEMC to determine rather than being a core component of the rule change request. We consider that consumer protections should be expressly outlined early in the consultation process rather than being established gradually alongside the rest of the rule change.



## Conclusion

Shell Energy does not consider that the FTA rule change would meet the National Electricity Objective or the National Energy Retail Objective. We have many concerns around the potential impacts to reliability, price, and consumer protections. We argue the costs of the reform are likely to be passed onto all consumers for the potential benefit of a small subset of customers.

Chiefly though, we note that there are a number of opportunities open to customers now that allow them to access FTA-like arrangements. These bring into question the need for the FTA rule at all and the supposed value benefits, given they are accessible now and do not come with the need for costly regulatory reform, and include:

- SGA framework
- Virtual Power Plants
- WDRM

Shell Energy has developed a LoadFlex product which leverages these existing structures to allow us to optimise the CER of non-retail customers and obtain benefits from demand response, Frequency Control Ancillary Service markets, and network tariff optimisation. This does not require further regulatory change.

In addition, Shell Recharge Solutions offers a product in the EU allowing non-Shell retail customers to have EV charging costs billed to Shell rather than their existing retailer. We consider this should be possible in Australia without the need for regulatory change.

In the case of the WDRM, increasing the number of methodologies open for customers to access could provide further value. This would be far lower cost and present far fewer risks to consumers than the FTA proposal. Shell Energy recommends new methodologies should be prioritised as an alternative to FTA.

For more detail on this submission, please contact Ben Pryor, Regulatory Affairs Policy Adviser ([ben.pryor@shellenergy.com.au](mailto:ben.pryor@shellenergy.com.au) or 0437 305 547).

Yours sincerely

[signed]

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