

22 August 2024

Anna Collyer
Chair
Australian Energy Market Commission
GPO Box 2603
Sydney NSW 2000

Submitted via: <https://www.aemc.gov.au/contact-us/lodge-submission> (EPR0097)

Dear Ms Collyer,

AEMC Electricity pricing for a consumer-driven future: Draft Terms of Reference

Nexa Advisory welcomes the opportunity to provide a submission on the AEMC's *Electricity pricing for a consumer-driven future* Draft Terms of Reference (EPR0097). The AEMC has initiated this Review itself to address the fact that current pricing arrangements were designed for a one-way electricity system and inelastic consumer demand.

Nexa is a 'for purpose' advisory firm. Our unwavering focus is accelerating the clean energy transition in a way that provides secure, reliable, and affordable power for consumers of all types. Nexa Advisory is a team of experienced specialists in the energy market, policy and regulation design, stakeholder engagement, and advocacy. We work with public and private clients including renewable energy developers, investors and climate impact philanthropists to help them get Australia's clean energy transition done.

We broadly support the scope of the Review, which is long overdue¹ and the key focus areas outlined by the AEMC are appropriate:

1. Market arrangements that provide for consumer choice between a range of appropriate products, services, and associated prices that suit their needs and preferences.
2. The role of distribution networks in enabling the right products, services, and incentives for consumers, and the efficient cost and pricing outcomes that result.
3. The role of retailers and energy service providers in effectively packaging and pricing electricity products and services to match consumer preferences.

We suggest that these areas should be considered through four lenses:

- Governance, the allocation of responsibilities and the interaction between all market participants and broader stakeholders
- The development of CER opportunities, product and service markets
- The role of regulation and competition in these areas
- Consumer value

In this submission, we provide some of the key areas of interaction that must be taken into consideration as part of this Review.

¹ <https://nexaadvisory.com.au/web/wp-content/uploads/2023/10/Nexa-Distributed-Energy-Resources-paper-and-recommendations-04102023.pdf>

The overarching need for review

Nexa Advisory identified in its October 2023 report “Putting the Power in People’s Hands²” that DNSP tariffs were a critical focus area to support the uptake of Consumer Energy Resources (CER) and Distributed Energy Resources (DER).

Prior to the AEMC’s cessation of the annual Electricity Network Economic Regulatory Framework (ENERF) Review in 2020³, there was a regular opportunity for industry and stakeholders to address any issues with DNSP tariffs.

The annual ENERF Review was requested in 2016, by the then COAG Energy Council in response to the growth in CER⁴. The ENERF review was an important tool for the federal government and state energy ministers to monitor and direct work on key distribution issues. The absence of the ENERF review over past 4 years, and in a CER context that is changing more rapidly than in 2016, has resulted in outcomes that are detrimental to consumers. This has included export tariffs and emergency backstops⁵.

A follow up Nexa Report in May 2024⁶, further demonstrated the lack of innovation in network tariffs and the absence of a focus on the expectations of consumers with regards to the treatment of the CER.

However, while this Review will explore “the incentives, roles, responsibilities, and technical requirements of retailers and distribution network service providers”, it will also be essential to explore how the *interaction* between DNSP tariffs and retailer tariffs may or may not support consumer responsiveness and flexibility.

Enhancing competition and innovation

CER poses challenges to the business models of incumbent energy market participants, encompassing electricity distribution and transmission networks, retailers, and large-scale generators. It disrupts established retail markets and necessitates the development of new, innovative business models to accommodate its flexibility and potential.

While smaller energy service providers are entering the market, many struggle to thrive within the existing retail ecosystem. The recent energy crisis witnessed numerous newer retailers exiting the market, highlighting the challenges faced by smaller retailers⁷.

The current regulatory framework often favours incumbents, limiting the evolution and competitiveness of new entrants and the development of technology solutions they bring. There is a need to reassess the roles of traditional and innovative players in the energy retail landscape.

² <https://nexaadvisory.com.au/web/wp-content/uploads/2023/10/Nexa-Distributed-Energy-Resources-paper-and-recommendations-04102023.pdf>

³ https://www.aemc.gov.au/sites/default/files/documents/epr0085_-_enerf_2020_-_final_report_for_publication_1_oct_2020.pdf

⁴ <https://www.aemc.gov.au/market-reviews-advice/electricity-network-economic-regulatory-framework-review-2020>

⁵ <https://nexaadvisory.com.au/web/wp-content/uploads/2023/12/Cutting-off-solar-isnt-the-answer-18-Oct-2023-1.pdf>

⁶ https://nexaadvisory.com.au/web/wp-content/uploads/2024/05/Nexa-Advisory-_Accelerating-CER-in-Australia.pdf

⁷ <https://www.accc.gov.au/media-release/electricity-retailers-under-pressure-as-contract-markets-tighten-and-prices-rise-further#:~:text=Smaller%20electricity%20retailers%20are%20finding,latest%20Electricity%20Market%20Inquiry%20Report>

Competition and innovation are essential for fostering a decentralised energy future and supporting the flexibility offered by CER. Addressing market power imbalances in the retail sector is crucial to ensure that customers have access to a diverse range of innovative services and solutions.

The Review should consider the initiatives currently underway to support this – by market bodies, incumbent and new entrant retailers, TNSPs and technology solution providers. This spans demonstrations and trials such as Project Symphony, Edge and the CER Data Exchange⁸, as well as other market-led initiatives. The AEMC should undertake a ‘market sounding’ engagement (or alternatively scope this as part of the Reference Group) during the early stage of this Review to understand these various initiatives. This would enable the assessment of competitive dynamics and neutrality extant in today’s market, and inform the broader elements of the Review.

Consumer Preference Principles

The AEMC indicates in the Terms of Reference that it will apply a “set of consumer preference principles” to inform the development of pricing solutions. However, these “Consumer Preference Principles” are not defined in the Terms of Reference and has not outlined how these Principles will be designed and developed.

It will be critical that Consumer Preference Principles are developed as the first priority of the Working Group, and publicly consulted upon before being finalised. These Principles will necessarily shape the final outcomes of the Review, which will have a significant impact on all consumers, with or without CER. The Principles should reflect both the desired outcomes of consumers and the potential competition in the market that new energy providers will drive.

The AEMC must carefully consider how these Principles impact their assessment. We note there may be difficulties associated with a consumer preference-led approach given preferences change over time and may not accurately reflect hard-to-measure elements such competitive dynamics, option value for consumers and equity. We also caution the Review applying an overly narrow focus to these Principles in assessment. For example, as part of a piece of work Nexa Advisory is currently undertaking (assessing the current regulatory process for large-scale projects), we have found that while regulatory principles may align with the consumer-focused objectives of efficient and prudent outcomes, they can contribute to unintended consequences if they are the sole criteria in assessment.

Interaction between DNSP and retailer tariffs

Currently, only the DNSP is aware of the constraints and capacity of their networks operationally. Network tariffs, along with Dynamic Operating Envelopes, may be used to signal network availability, but those tariffs are then mediated through the retailer, which may or may not obscure the network signal.

The retailer or energy service provider has a critical role in operationalising a network tariff to ensure a lower cost system. Whether a consumer is price responsive or not is a choice for the consumer to make through the selection of retail tariff that is appropriate to them. Larger

⁸ <https://aemo.com.au/initiatives/major-programs/nem-distributed-energy-resources-der-program/markets-and-framework/CER-Data-Exchange-Industry-CoDesign>

consumers may have a direct relationship with their DNSP and may be exposed to specific network tariffs, but typically the DNSP-customer relationship is mediated via the retailer.

The AEMC needs to explore the roles and responsibilities of all parties in the pricing dynamic, understanding how the DNSP-retailer, DNSP-Aggregator and DNSP-Service Provider relationships need to change to facilitate the orchestration of CER. The Review needs to develop a baseline of roles and responsibilities and determine whether these are appropriate for today and the in the future. Any new arrangements need to be robust to future developments and supportive of new innovative players and approaches, as this will drive competition and benefits for consumers.

We consider that ring-fencing is likely to form a significant part of this Review and may be appropriate to address as a distinct workstream (similarly to contestability within the Transmission Planning and Investment Review).

The need for social licence

While the AEMC recognises the ongoing work to secure social licence for new large-scale renewable generation projects and new transmission lines, it does not recognise the importance of social licence for consumer energy resources in allowing these to be utilised for system flexibility and support.

Nexa Advisory is concerned that AEMO and market participants more broadly continue to pursue the notion that significant CER capacity can be leveraged to provide flexibility to support secure system operation. The industry's current approach must be viewed in the context that consumers are very reluctant to countenance 'orchestration'^{9,10} and that consumers have a significant lack of trust in the energy sector generally¹¹.

Further, the current draft decision from the AEMC on Integrating Price-Response Resources (IPRR) into the NEM¹² will further erode consumer-industry trust. This would allow the Financially Responsible Market Participant (FRMP), typically the retailer, to decide whether any given consumer's CER should be dispatched, with no additional protections on engaging with the consumer that owns the CER.

The benefits of orchestration in aggregate may represent a significant cost reduction in operating the system overall^{13,14}, but at the individual consumer level such approaches may have minimal benefits either in terms of control of the CER or in terms of remuneration for ceding control¹⁵.

New pricing arrangements must recognise the difference between the system-wide benefits versus the individual consumer benefits of orchestration. Any new pricing arrangements for DNSPs and retailers developed with the intention of facilitating orchestration must have consumer buy-in. This will need to be secured and maintained.

⁹ <https://aemo.com.au/-/media/files/initiatives/der/2022/community-perceptions-of-der-and-aggregation-services.pdf?la=en>

¹⁰ https://energyconsumersaustralia.com.au/wp-content/uploads/insight_behave_23_3.png

¹¹ <https://www.edelman.com.au/trust/2024/trust-barometer#download>

¹² <https://www.aemc.gov.au/sites/default/files/2024-07/Draft%20Determination.pdf>

¹³ <https://aemo.com.au/-/media/files/major-publications/isp/2024/2024-integrated-system-plan-isp.pdf?la=en>

¹⁴ https://www.aemc.gov.au/sites/default/files/2024-07/240725%20-%20AEMC%20-%20Draft%20Terms%20of%20Reference%20%28publication%29_0.pdf

¹⁵ <https://www.energynetworks.com.au/assets/uploads/The-Time-is-Now-Report-ENA-LEK-August-2024.pdf>

As such, we support the consumer-centric approach of this Review and encourage social acceptance to be included in the Consumer Preference Principles and throughout the Review.

Without DNSP data, pricing isn't transparent

In the context of a lack trust between consumers and industry, it is critical that consumers and third-party providers of services and technology have access to distribution network data.

Consumers are concerned about the increasing cost of electricity, while already struggling with a broader cost of living crisis. The network cost element of the electricity bill represents up to 45 per cent of the total bill, with DNSP costs growing rapidly¹⁶. DNSPs are seeking to erode the protections provided by the Ringfencing arrangements, by utilising network assets paid for by consumers to grow shareholder income, such as providing Reserve Energy Reliability Trader (RERT) services¹⁷ and investing in “community” batteries¹⁸, without sharing the income to benefit consumers.

DNSPs favour capital investment solutions that enhance the Regulated Asset Base and revenue, rather than non-network solutions, such as purchasing a service (operational cost), which are likely to be lower cost and are more flexible in a dynamic CER-driven future¹⁹.

Without transparent access to DNSP network data, it is not possible to identify where non-DNSP-led solutions could offer value. With the advancement of “digital twins”^{20,21}, DNSPs are able to identify capacity issues that could be resolved with a non-network solution. However, DNSPs are pursuing “anticipatory” network expansion, ahead of need²², even while declaring networks under-utilised²³. Consumers should pay no more than needed, no sooner than required²⁴.

The Energy Security Board (ESB) data strategy²⁵ identified a number of key data use cases and relevant stakeholders. To date, only access to the data needed by industry has been progressed as a priority^{26,27}. This focus needs to change to ensure that DNSP decisions are made transparently, where all parties have access to network data.

The Distribution Annual Planning Report (DAPR) is no longer fit-for-purpose as it focuses on zone sub-stations and does not accommodate the changes that have occurred and are accelerating at the consumer connection point²⁸. The DAPR is not the right vehicle to provide

¹⁶ <https://energyconsumersaustralia.com.au/news/newsletter-july-2024>

¹⁷ <https://www.aer.gov.au/industry/networks/ring-fencing/reliability-and-emergency-reserve-trader-rert-voltage-management-ring-fencing-class-waiver-december-2022>

¹⁸ <https://www.energynetworks.com.au/assets/uploads/The-Time-is-Now-Report-ENA-LEK-August-2024.pdf>

¹⁹ https://nexaadvisory.com.au/web/wp-content/uploads/2024/05/Nexa-Advisory_-_Accelerating-CER-in-Australia.pdf

²⁰ <https://www.essentialenergy.com.au/media-centre/media-release/news-7-digital-twin>

²¹ <https://www.endeavourenergy.com.au/news/media-releases/endeavour-energy-pioneers-neara-digital-twin-in-transition-to-modern-grid>

²² <https://www.energynetworks.com.au/assets/uploads/The-Time-is-Now-Report-ENA-LEK-August-2024.pdf>

²³ <https://www.energynetworks.com.au/assets/uploads/The-Time-is-Now-Report-ENA-LEK-August-2024.pdf>

²⁴ <https://energyconsumersaustralia.com.au/news/newsletter-july-2024>

²⁵ <https://www.aer.gov.au/system/files/ESB%20-%20Network%20Visibility%20-%20July%202023.pdf>

²⁶ https://nexaadvisory.com.au/web/wp-content/uploads/2024/05/Nexa-Advisory_-_Accelerating-CER-in-Australia.pdf

²⁷ <https://nexaadvisory.com.au/web/wp-content/uploads/2024/07/Nexa-Advisory-submission-AEMC-Accelerating-Smart-Meter-Deployment.pdf>

²⁸ https://nexaadvisory.com.au/web/wp-content/uploads/2024/05/Nexa-Advisory_-_Accelerating-CER-in-Australia.pdf

the necessary data to help new energy services providers and other third-parties identify where their services may support network operation. Urgent reform to support data sharing is needed.

Without public access to network data, it will never be clear if capital investment is needed by the DNSP, or whether there are other non-network and third-party led options that would allow consumers to actively support network operation at a lower cost. Without this transparency, trust in the industry and in DNSPs can never be developed, preventing innovative, cost-effective solutions, such as orchestration, from being delivered. This further undermines the social licence for pricing and ability to implement much needed tariff reform.

As such, we consider that the role of distribution network planning and operational data arrangements in facilitating the uptake of CER should be a core workstream of this Review. A key outcome of this workstream could be to quantify the cost of the information asymmetry described above in terms of the adverse impacts this will have on the uptake of CER into the future.

Thank you for the opportunity to provide input on the Draft Terms of Reference. We welcome the opportunity to further discuss any aspect of our submission and look forward to continued engagement through this work.

Yours Sincerely

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