



7 October 2021

Harrison Gibbs
Australian Energy Market Commission
GPO Box 2603
Sydney NSW 2001

Lodged via: <https://www.aemc.gov.au/contact-us/lodge-submission>

Dear Mr Gibbs

RE: Review of compensation guidelines to include wholesale demand response (EPR0088)

Shell Energy Australia Pty Ltd (Shell Energy) welcomes the opportunity to respond to the Australian Energy Market Commission's (AEMC's) draft amendments to the compensation guidelines (the Guidelines) to incorporate wholesale demand response (WDR).

About Shell Energy in Australia

Shell Energy is Australia's largest dedicated supplier of business electricity. We deliver business energy solutions and innovation across a portfolio of electricity, gas, environmental products and energy productivity for commercial and industrial customers. The second largest electricity provider to commercial and industrial businesses in Australia¹, we offer integrated solutions and market-leading² customer satisfaction, built on industry expertise and personalised relationships. We also operate 662 megawatts of gas-fired peaking power stations in Western Australia and Queensland, supporting the transition to renewables, and are currently developing the 120 megawatt Gangarri solar energy development in Queensland. Shell Energy Australia Pty Ltd and its subsidiaries trade as Shell Energy.

www.shellenergy.com.au

General comments

Shell Energy is broadly supportive of most of the AEMC's proposed changes to the Guidelines. However, we believe some of the criteria related to valuing opportunity costs, particularly for demand response service providers, is unnecessarily complex. This submission explores the relevant criteria and proposes a simpler alternative. We believe our proposed suggestions would result in compensation more accurately reflecting the cost to impacted parties.

Opportunity costs for demand response service providers

Section 7.2 of the draft Guidelines stipulates that, in order to make a claim for opportunity costs, the claimant must:

1. demonstrate that its plant has scarce capacity
2. calculate the value of the more profitable alternative.

¹ By load, based on Shell Energy analysis of publicly available data.

² 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 2011-2020.



The draft Guidelines go on to provide additional guidance in relation to opportunity costs claims from demand response service providers (DRSPs):³

1. *"The AEMC may consider additional factors including (but not limited to) whether the price and quantity response points and other information provided in dispatch, pre-dispatch and short term projection of system adequacy (ST PASA) during the administered price limit event are consistent with the typical information and operation of the wholesale demand response unit during the normal function of the market. For example if the DRSP bids and is dispatched to provide wholesale demand response when the energy price is capped at \$300/MWh, but it usually offers wholesale demand response only at significantly higher prices, the DRSP would need to explain why it should be eligible for any compensation.*
2. *Commercial losses resulting from lower production of products other than wholesale demand response or market ancillary services (eg if the wholesale demand response unit is a factory, reduced production of goods by the factory), while dispatched during an administered pricing period, can only be claimed at price and quantity response points that are consistent with the typical operation of the relevant wholesale demand response units when it is not providing wholesale demand response.*

The claimant will need to provide sufficient evidence justifying its claim in regards to the factors above. The Commission notes that claims will be made on a case-by-case basis with the ability not to follow the guidelines if there is sufficient reason not to."

In our view, this guidance is unnecessarily complex. Because the burden of providing "sufficient evidence justifying its claim" is on the claimant, claimants may incur inefficiently high compliance costs trying to substantiate legitimate claims. Similarly, it may be challenging for the AEMC to assess the extent to which claimants have been genuinely impacted, or whether they are 'gaming' the compensation framework.

As an alternative, we suggest replacing the above guidance for DRSPs with a provision (that would relate to all participants) to the effect of:

"The dispatch bids provided by the participant will be taken to reflect the total opportunity costs for the participant during those trading intervals for which a claim for additional compensation has been lodged. All claims for additional compensation will be assessed and capped based on a participant's dispatch bids."

We believe this provision would be best located directly under section 7.2 of the draft Guidelines (prior to section 7.2.1), after the second dot point. In doing so, a participant's dispatch bid would be taken to represent the total costs of providing dispatchable services for the purpose of calculating compensation.

Our suggested insertion would meet our understanding of the AEMC's intent: to prevent market participants from 'gaming' the regulatory framework, while still allowing for fair compensation. Our rationale is as follows:

- During an administered pricing period (or any other period where market suspension pricing has been invoked), dispatch is maintained (where possible) on the basis of marginal costs. Price discovery of marginal costs is from participants' dispatch bids. Settlement prices are then adjusted post calculation of dispatch either in line with the administered price cap, administered price floor or the market suspension pricing schedule. This applies to both NEMDE scheduling of dispatch and (where possible)

³ AEMC, *Draft amended compensation guidelines, Proposed guidelines*, 26 August 2021. Accessed from: https://www.aemc.gov.au/sites/default/files/documents/draft_amended_compensation_guidelines_0.pdf



AEMO manual scheduling of dispatch, where AEMO is required to dispatch the lowest-cost assets to achieve the power system needs at that time.

- If the market is competitive, a participant's dispatch bid will theoretically be their opportunity cost (assuming a scarce resource). With this in mind, there are several scenarios in which our suggestion is relevant.
 - If a participant reduces their dispatch bid in order to gain dispatch and be eligible for compensation, this would be interpreted as the participant declaring a reduction in their opportunity cost. This would help to maintain dispatch efficiency by disincentivising 'race to the floor' bidding that can result in higher marginal cost assets being dispatched ahead of lower-cost assets.
 - If a participant is not dispatched (regardless of whether they increase, reduce or do not alter their dispatch bid), then they would not be eligible to make a claim for additional compensation, as no economic losses at dispatch have occurred.
 - If a participant increases their dispatch bid and is dispatched, their claim would be capped using the price of their bid. Additionally, the participant would still be required to fulfill the obligations imposed by section 7 of the draft Guidelines. For example, consider a scenario where transient market power may exist and a participant rebids capacity to the market price cap (MPC). In order to receive compensation equal to the difference between the received price (e.g. the administered price cap) and the MPC, the participant must meet the section 7 data requirements to show that its bid (at the MPC) reflected its true opportunity cost.
 - If a participant does not alter their dispatch bid and is dispatched, then they would be eligible for compensation, capped at the price of their bid. Because the bid price remains unaltered, we consider it would be relatively simple for the participant to justify (and the AEMC to assess) that their bid reflected their opportunity costs, based on the existing section 7 information obligations.

If you would like to discuss this submission further, please contact Ron Logan, Senior Markets Adviser at ron.logan@shellenergy.com.au or on 0427 002 956.

Yours sincerely

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