

18 May 2020

Dr Kerry Schott AO
Independent Chair
Energy Security Board

Submitted via email: info@esb.org.au

Dear Dr Schott

Stanwell Response to Consultation on Two Sided Markets

Stanwell appreciates the opportunity to provide feedback on the Energy Security Board's (ESB's) consultation paper on two-sided markets.

However, Stanwell notes the timeframe to assess and respond to this discussion paper was constrained, particularly considering the impacts that COVID-19 is having on staffing and working arrangements of industry participants.

Please note, this submission contains the views of Stanwell Corporation Limited in relation to the two-sided markets information provided to date and should not be construed as being indicative or representative of Queensland Government Policy.

1. Introduction

Stanwell appreciates the ESB's interest in increasing demand-side visibility and participation in the market, and that it is undertaking work to determine how this could be facilitated.

However, it does not appear that this work is sufficiently integrated with the other significant work currently underway in the ESB's Post-2025 Market Design project. In addition, it is Stanwell's view that the consultation paper does not account for the considerable benefits of earlier stages of participation (primarily increasing visibility at the transmission network level, and then increasing net visibility at the meter) and overstates the appetite and ability of households to materially participate in the wholesale electricity market.

2. Integration with other regulatory reform

Stanwell is concerned about both the speed at which such a significant market reform is being progressed and the lack of visible integration with the other work streams underway, including those forming the ESB's Post-2025 Market Design project.

The tight timeframes and concurrent development will limit the ability of the market bodies and participants to identify interdependencies, opportunities and inconsistencies between the individual work streams. These interdependencies mean feedback on individual work streams is not a substitute for feedback on the package of market reforms as a whole.

For example, at the transmission network level a two-sided market will essentially require a redesign of the current COGATI proposal. It should first be determined what version of the two-sided market will be pursued prior to progression of access reform.

At the pricing and risk management level there is a question relating to what incentives are trying to be imposed on the market. The Retailer Reliability Obligation (RRO) aims to incentivise appropriate and timely new entry by encouraging retailers to purchase hedges on behalf of consumers. On the other hand, the Demand Response Mechanism (DRM) appears to encourage consumers and their representatives to take and manage spot exposure. Without a clear intent as to what outcomes regulation is attempting to drive it is extremely difficult to define what success will look like, let alone measure it.

We understand that the ESB has been working with the market regulatory bodies on prioritising the extensive market reform and rule change work program that is underway. This reprioritisation work aims to identify opportunities to better align and coordinate initiatives, in response to the COVID-19 impacts. We encourage the ESB to continue to engage with the market bodies as the regulatory reform reprioritisation work progresses and develop options that would allow industry more fulsome consideration of related and interdependent reform proposals that are currently under development.

3. Partial versus full participation

The consultation paper notes *“[t]he full participation model should be the goal for a two-sided market as it would provide the most information to the market operator and elicit the most value from responsive capabilities in the market. However, consideration needs to be given to whether there should be a market-wide change at a given point, or some transition towards full participation.”* (page 21).

Stanwell believes further exploration of the staged roll-out of demand side participation in a two-sided market is warranted. This would assist in determining both the pre-requisites for expanding participation from large users to smaller users (e.g. technology, tariffs, consumer protections), the expected benefits and costs associated with each stage of increased participation, and the appetite and barriers to entry for different types and sizes of consumers to participate in the wholesale market.

Stanwell suggests that most of the benefits of increased demand side participation would be realised through the selective participation model discussed briefly in the consultation paper. As the consultation paper notes, large energy users *“represent around 66 per cent of overall demand in the NEM, but only make up 0.8 percent of total connection points in the NEM”* (page 20). These sophisticated energy users have both the ability to shift energy use and the scale to impact the market when they do so. By comparison, while some individual residential households may have the incentive and ability to respond, kilowatt level changes will not be visible to the market operator unless significantly aggregated.

Scheduling large loads would significantly increase AEMO's visibility of the demand side at the transmission network level and avoid the potential negative impacts on the market of non-scheduled demand-side participation.

Following successful implementation and evaluation of the selective model of participation, the further roll-out (i.e. increased net visibility at the meter, then full participation of the type detailed in the consultation paper) could be examined.

Moving to implementation and operation costs, the consultation paper notes "*full participation model would likely be the costliest to implement, as an obligation to understand, and bid in intentions would apply to all participants*" (page 21).

Stanwell would like to see evidence or modelling that shows that the higher costs of full participation are more than offset by benefits for consumers. If this is not the case, Stanwell's position that greater net benefits would be realised at a lower level of participation merits an alternative approach to implementation.

4. Household appetite

Further consideration of the appetite of households to participate in the market is also required. Stanwell contends that many households have limited appetite to participate in the wholesale electricity market. Households generally favour simple and hassle-free energy service where retailer manage their exposure to market fluctuations on their behalf and minimise the complexity of product offerings. This is evidenced by the high number of customers remaining on default offers, and low customer switching rates. We also contend that many customers have a limited ability to shift demand without a sizeable loss of utility.

There are also distributional impacts of full participation. Low income households may be unable to afford electricity at times when high income households are willing to pay more. Further investigation of the distributional impacts and mechanisms to ensure low income households are not excluded from an essential service will be required as part of future iterations of the proposed two-sided market.

The consultation paper also notes "*[m]ost traditional markets are two-sided such as commodity and agricultural markets. There is currently an opportunity for the NEM to shift away from being like a one-sided market and move towards being a two-sided market.*" (page 4).

While some large energy users participate in two-sided commodity and agricultural markets, households are not currently active participants in these types of markets. Stanwell questions the applicability of this type of market model to households for procuring electricity (an essential service about to move to five-minute price intervals).

5. Conclusion

Stanwell supports reform that will enable increased demand side participation in the NEM, but considers the scale and scope of a two-sided market as presented in the consultation paper does not adequately evaluate the potential for higher net benefits from less than full participation. In addition, Stanwell encourages the ESB to better align this initiative with its Post-2025 Market Design project that is currently underway.

Stanwell welcomes the opportunity to further discuss this submission. Please contact Evan Jones on (07) 3228 4536.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'I. Chapman', with a long horizontal flourish extending to the right.

Ian Chapman
Manager Market Policy and Regulatory Strategy