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Dr Kerry Schott AO

Chair, Energy Security Board

Submitted by email: info@esb.org.au

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Consultation on Retailer Reliability Obligation Legislative Amendments

Dear Dr Schott,

AGL Energy (**AGL**) welcomes the opportunity to make a submission in response to the Energy Security Board's (**ESB**) Consultation on Retailer Reliability Obligation Legislative Amendments (**Amendments Paper**).

AGL is one of Australia's largest integrated energy companies and the largest ASX listed owner, operator and developer of renewable generation. Our diverse power generation portfolio includes base, peaking and intermediate generation plants, spread across traditional thermal generation as well as renewable sources. AGL is also a significant retailer of energy, providing energy solutions to around 3.5 million customers throughout eastern Australia.

In addition, AGL is continually innovating our suite of distributed energy services and solutions for customers of all sizes. These behind-the-meter energy solutions involve new and emerging technologies such as energy storage, electric vehicles, solar PV systems, digital meters, and home energy management services delivered through digital applications.

A long-term approach to energy policy

The piecemeal introduction of carbon reduction and renewables policies has produced unintended consequences for wholesale energy markets, as price signals and incentives for development have shifted over time. The lack of a long-term mechanism to address emissions reductions that has bipartisan political support has been a significant contributor to increased risks and costs for energy market participants and has had material impacts on the Australia energy sector overall.

AGL has therefore consistently asked for governments and policy makers to bring a long-term vision to energy market reform. The transition of the energy market must be supported by a strategic framework that aims to minimise negative impacts while simultaneously maximising opportunities for net positive impacts from the transition for all stakeholders.

The electricity sector has already experienced significant disruption over the last decade, most notably from declining demand that was poorly forecast and the disorderly exit of thermal plant replaced by subsidised large-scale renewables. This disruption has led to numerous enquiries including the Finkel Review (principally addressing security and reliability) and the ACCC's Price Inquiry (principally addressing price), which have provided a number of recommendations for reform, many of which are already well progressed.

This increased attention on the operation of the NEM has led the development of a number of significant alterations to the operation of the market including the progression of five-minute settlement, actioning of the Integrated System Plan, the development of a demand response mechanism, an enhanced RERT, a closure rule, ancillary service framework reviews, and proposed changes to competition law specifically applying to the energy sector.



The composite impact of these reforms will require close monitoring to ensure the objectives of security, affordability, and sustainability in a carbon-constrained future are met at least cost. As the transition continues, it will remain a topic for discussion if the operation of the NEM remains fit for purpose to provide the most efficient mix of sustainable and reliable generation at the lowest price for customers.

Our approach to power station development and closure is guided by these aims, but what is missing from our ability to invest in the future is long-term certainty from the Government on the trajectory of decarbonisation in the electricity sector and the reliability settings under which that will occur. This uncertainty drives up wholesale costs, leads to the inefficient deployment of capital, delays investment, and impacts on the ability to assist in the optimal transition for communities experiencing change.

In seeking to establish this long-term certainty, AGL has therefore supported the ESB's efforts to develop a framework that integrates emissions reductions policy with energy policy through the draft design of the National Energy Guarantee (**NEG**), and to establish a clear trajectory and policy mechanism to reduce Australia's greenhouse gas emissions over time under fixed reliability settings.

The role of the RRO

The NEG was primarily a mechanism to provide certainty on investment trajectory during a period of transition to lower emissions generation sources, with an associated safeguard to support system reliability. The Retailer Reliability Obligation (**RRO**) is the evolution of this safeguard and its design should therefore focus on meeting this aim. However, it should be noted that the design of the reliability component of the NEG was to work in tandem with an emissions reduction obligation. Removing the emissions component of the NEG will also remove a key policy component that was designed to drive long-term investment.

As more renewables enter the market and proposed renewable energy zones are connected to the NEM through further interconnection, existing thermal generation will eventually exit the market as it reaches the end of its design life and becomes increasingly underutilised. Within this framework, the RRO may assist in maintaining system reliability on a year on year basis, with emergency reliability continuing to be managed by the RERT emergency reserve mechanism. However, we note that the RRO is as yet untested, and its impact in terms of underpinning longer-term investment and assisting with the orderly closure of aging plant will need to be monitored to understand whether it meets the expectations of policy-makers.

AEMO's forecasts of future market conditions are the basis for the trigger of the RRO and the continuing procurement of the RERT. Therefore, improving the accuracy of these forecasts will be important and should be prioritised, noting that the forecast will always be somewhat uncertain due to probabilistic inputs regarding maintenance, availability, and prevailing weather conditions. The forecast reliability standard may therefore also need to be reviewed to reflect the value of reliability and the objectives of the RRO.

We note that this and many other important conditions under which the RRO will operate are anticipated to be the subject of future Rules consultations. We look forward to participating in the development of those Rules, and in particular those that will provide further clarity on what will constitute a material reliability gap and how liable entities' contracts will be calculated to establish that their obligation has been met.

We have some apprehension regarding the detail of the RRO that is proposed to be in the National Electricity Law (**NEL**). Reliability obligations on purchasers of energy are untested in their operation, and much of the success of the RRO will depend on the settings of the mechanism, which are difficult to place within such an uncertain environment. Elements such as the strength of the hedging requirement may therefore be better set out in the Rules along with other conditions of the framework such as the calculation of firmness factors and the definition of a material reliability gap. In our view, these settings may need to be adjusted over time to meet the objective of the RRO and the flexibility to make those amendments may be better suited to the Rules or another subsidiary legislative instrument.



We also have some concern about the necessary pre-conditions to trigger the RRO. For example, the provision to allow the AER to make a T-1 reliability instrument without a related T-3 reliability instrument (Section 14H(2)(b)) seems to be in contradiction to the design of the RRO, which necessitates a sufficient lead time for retailers to react to a shortfall by entering into firm contracts.

While the ESB has stated that this exemption should be made available for flexibility, we consider that the appropriate mechanism for maintaining reliability at short notice (i.e. less than two years), could also be a well defined and efficient RERT mechanism. The interaction between the RRO and the RERT will therefore need to be examined closely. While there may be occasions where it is appropriate to trigger the RRO at short notice, we consider that these conditions must be predictable and set out clearly for participants to be able to factor that risk into their operations. Where the RRO is triggered with less than three years notice, there should be commensurate flexibility to adjust the obligations on participants to take account of the lower lead times for compliance, which could also be clearly established in Rules regarding this process.

Next Steps

AGL remains committed to supporting policy that provides clear long-term investment signals for the electricity sector in terms of expected commitments to reduce emissions. Where this trajectory may produce unintended consequences, for example, in terms of system reliability and security, we support reforms that are targeted to efficiently balance the outcomes required.

We are hopeful that State and federal Governments will work collaboratively in the future to achieve these aims for the benefit of customers, the environment, and the broader Australian economy.

Should you have any questions in relation to this submission, please contact Aleks Smits, Manager Policy & Research on 03 8633 7146, or myself on 03 8633 7252.

Yours sincerely,

A handwritten signature in blue ink, appearing to be 'Eleanor McCracken-Hewson', written over a horizontal line.

Eleanor McCracken-Hewson

Senior Manager Policy, Research & Stakeholder Engagement, AGL Energy