



BlueScope Steel Limited  
ABN 16 000 011 058  
11/120 Collins Street  
Melbourne VIC 3000  
PO Box 18207  
Collins Street East  
Melbourne VIC 8003  
Telephone +61 3 9666 4000  
Facsimile +61 3 9666 4111  
[www.bluescope.com](http://www.bluescope.com)

13 July 2018

## National Energy Guarantee

### Submission on the Draft Detailed Design Consultation Paper and Technical Working Papers

BlueScope Steel (**BlueScope**) welcomes the opportunity to provide comments in response to the Energy Security Board on the draft detailed design of the National Energy Guarantee (**Guarantee**).

BlueScope is Australia's largest steel manufacturer and the only flat steel producer. We employ 6,500 people in Australian regions and cities to supply our nationwide customers in the building and construction, manufacturing, transport, and agriculture sectors. BlueScope also exports steel products and is a global leader in premium coated and painted steel products, operating in 17 countries.

BlueScope is very concerned that electricity has become increasingly unaffordable and potentially unreliable for large, energy-intensive manufacturers.

As a large electricity consumer, energy affordability, reliability and security are fundamental to the competitiveness of our business. Over recent years, BlueScope has transformed its operations to return to profitability. Keeping domestic production costs competitive remains paramount and energy is a major cost in steelmaking. Rising energy costs represent the single largest increase in BlueScope's local production costs. More expensive energy directly affects our capacity to invest and provide employment. As such, the Guarantee's aim of lowering the cost of electricity to customers is central to our support for the policy.

Historically, issues of electricity supply and reliability have not been regarded as particularly high risks to BlueScope's Australian operations, largely due to the significant reserve capacity within the National Electricity Market (NEM). However, recent assessments showing a reduction and potential shortfalls in the dispatchable capacity in the NEM, along with load shedding events last year, raise concerns about energy reliability for BlueScope's process-critical operations.

### Executive Summary

BlueScope supports the aim of the Guarantee to deliver more reliable, affordable and cleaner energy to Australian consumers and welcomes this consultation on the detailed design of the Guarantee. The company also supports Australia's 2030 emissions target, including the Australian government's goal to reduce emissions in the electricity sector by 26 per cent on 2005 levels by 2030.

BlueScope believes that an effective Guarantee must:

- Deliver a material and sustainable reduction in electricity costs to all consumers in order to support and promote domestic investment and employment;
- Promote lowest cost reliability, abatement (in line with Australia's 2030 target) and compliance;
- Provide clear policy and investment signals to build an appropriate level of future dispatchable generation capacity;
- Have a positive impact on market efficiency and maintain market liquidity;
- Not reduce competition or increase the concentration of market power in the energy sector;

- Maintain flexibility for large energy users to manage electricity costs; and
- Safeguard emissions-intensive trade-exposed industries (EITEs) from costs that jeopardise their competitiveness.

BlueScope commends the significant work that the ESB has carried out to date in progressing towards a workable policy. However, there are some key design elements that will require adjustment to ensure that the Guarantee delivers on its objectives:

- Emissions Reduction Requirement
  - The ESB should provide a user opt-in mechanism in the design of the emissions reduction requirement.
  - BlueScope supports the inclusion of non-market embedded generation as eligible generation under the Emissions Reduction Requirement but proposes that the threshold be aligned with the threshold under the RET for large-scale generation.
  - The Emissions Registry will provide an instrument to coordinate compliance; however, it should be open to all interested parties to aid in the development of a deep, liquid and competitive carbon market and, support lowest cost compliance.
  - BlueScope supports the measured use of flexible compliance options where it does not reduce required investment in electricity generation. The ESB should also consider providing two-way flexibility to allow emissions offsets in excess of the target under the Guarantee to be used to offset carbon in other parts of the economy.
  - With respect to the Commonwealth elements of the design:
    - BlueScope strongly supports the Commonwealth's position to provide EITE industries with an exemption under the Emissions Reduction Requirement.
    - BlueScope is supportive of the approach proposed by the Government to streamline the RET and Guarantee exemption application processes.
    - BlueScope acknowledges the need to reduce the uncertainty created by regular changes to emissions targets. However, the materiality of the inaccuracy and impact on the cost of the scheme to customers must be considered in setting the review period and process for review.
    - Access to offsets is supported however only at a level where they do not reduce or delay investment in reliable lower emissions generation technology.
- Reliability Requirement
  - BlueScope supports the ESB's aim of providing optionality to large users; however responsibility for the reliability requirement in respect of non-market C&I customers should lie by default with retailers. BlueScope proposes that all energy users be given the flexibility to opt-in and manage this obligation themselves, if they choose to do so.
  - The forecast timing of a reliability gap, trigger dates and measurement of liable entity's share of peak demand should be as granular and targeted as possible to ensure lowest cost compliance, regardless of the current form and availability of qualifying contracts. BlueScope would urge the ESB not to limit options for compliance by limiting the design to what is currently available in the contract market.
  - The proposed cut-off date of 20 April 2018 for the grandfathering provision does not recognise the significant time it takes to finalise a procurement strategy and enter into any power purchase agreement. Given the lack of information available on this provision up until the time of releasing the detailed design and the uncertainty in the COAG approval process, BlueScope proposes the cut-off date for contracts to qualify under the grandfathering provision should be the date that the detailed design is presented at the COAG Energy Ministers' Meeting in August 2018.
  - BlueScope is supportive of the Market Liquidity Obligation (MLO). We would suggest, however, that the ESB revisits its decision to not include caps, as this is again limiting the design to products currently available and potentially limiting the efficiency of the market to maintain reliability at lowest cost. BlueScope also believes the combination of the MLO with a trade repository (with reporting) would provide an optimal outcome for customers.
  - BlueScope supports the proposal for AEMO to administer a voluntary book build commencing at the T-3 trigger.
  - BlueScope supports the use of demand response contracts as a means of compliance under the reliability requirement. Work on developing a mechanism (as part of the AEMC's Reliability Frameworks Review) should be given priority by the ESB and AEMC.

BlueScope provides the following detailed feedback regarding several important elements of the detailed design:

## **Emissions Reduction Requirement**

### Entities covered by the emissions reduction requirement

The ESB is proposing that only market customers will be covered by the emissions reduction requirement.

BlueScope believes that large users should be provided flexibility under both the emissions and reliability requirement to manage the obligation themselves. A similar approach is already available and has worked well for many large users managing costs under the RET.

Therefore, BlueScope proposes that the ESB provide a user opt-in mechanism in the design of the emissions reduction requirement.

### Accounting for generation and load – non-market embedded generation and solar PV

The ESB proposes a capacity threshold of 5MW with respect to renewable non-market embedded generation. This precludes large scale solar under the RET between 100kW and 5MW from being included.

This cut-off may de-incentivise investment in renewable generation by commercial and industrial customers. BlueScope proposes that it is more beneficial to align the cut off for the Guarantee with the Large-Scale Generation Scheme eligibility size requirement to ensure consistency and maintain broader options for compliance.

The ESB has proposed that pre-1997 renewable generation that is largely composed of hydro generation be included under the Guarantee. BlueScope supports this position as it provides for a broader range of compliance options for liable entities. It also simplifies compliance and target setting under the Guarantee.

### Emissions Registry

BlueScope supports the development of a central Emissions Registry to ensure compliance is coordinated and at least cost.

The Emissions Registry design will play an important role in building market transparency and liquidity but the design as it is contemplated may inhibit the development of deep liquid and competitive markets that are essential in supporting compliance at lowest cost.

BlueScope proposes that, to support liquidity and competition, the registry be open to all interested parties (e.g. non-liable entities such as intermediaries and customers) to register and provide contracts to meet the emissions reduction requirement. The ESB's concerns on allocation can be addressed by simply requiring all account holders to balance load and generation assigned to their account, with penalties for non-compliance.

### Flexible Compliance Options

BlueScope supports the measured use of flexible design elements (carrying forward over-achievement, deferring compliance and using offsets) to ensure compliance at lowest cost.

As an extension of this principle, BlueScope proposes that the ESB consider providing flexibility to allow any excess emissions offsets created in the electricity sector to be used for offsetting emissions in other industries. Where the electricity sector can provide low cost abatement beyond that required to meet the target under the Guarantee, this abatement should be able to be used to offset emissions elsewhere in the economy. This will support lowest cost abatement across the economy and help build depth in Australian carbon markets.

## Other Considerations

BlueScope supports a nationally coordinated approach to reducing emissions in the electricity sector. It is appropriate that the emissions requirement will apply NEM-wide, but it seems equally appropriate that the same requirement should be applied all electricity networks in Australia (i.e. not just the NEM). Where state-based incentive schemes operate in addition to the RET, it is appropriate that the emissions target remains unchanged and retailers contracting with generators receiving subsidies through these schemes should be able to count their generation towards meeting the emissions requirement under the Guarantee.

However, BlueScope would strongly suggest that if a national coordinated approach is implemented for both emissions and reliability then State programs should be wound back and removed in a timely manner in order to prevent unintended consequences such as unnecessarily triggering reliability requirements by accelerating the rate of transition beyond that required to meet the target.

## Responses to consultation on Commonwealth Elements

For the purpose of providing a complete response to all elements of the design, this section outlines BlueScope's responses to the consultation paper provided by the Department of Environment and Energy on the Commonwealth elements of the Guarantee.

BlueScope strongly supports the Commonwealth Government's view that electricity used to carry out EITE activities should be exempt from the Emissions Requirement under the Guarantee.

This position is consistent with current exemptions under the RET and is aligned with the shielding provided under previous energy and emissions policy frameworks.

The rationale for providing assistance to approved EITE activities is that trade exposed businesses are competing in an international setting where their competitors do not face a similar impost. EITE businesses are unable to pass on the additional cost of energy and emissions regulations to their customers, and to remain competitive must absorb the additional costs. Preserving Australia's international competitiveness is essential to maintaining sustainable on-shore manufacturing operations and the provision of significant employment opportunities to Australians.

BlueScope acknowledges the historical level of rigor and analysis involved in defining and establishing approved EITE activities, and supports the position that to retain consistency, all EITE activities eligible for the exemption under the RET should be eligible for an exemption from the emissions requirement under the Guarantee.

Given the importance of the EITE exemption to the company, BlueScope would like to continue to provide input into the development of the legislation that will govern the exemption under the Guarantee.

## **Specific Responses to Questions:**

Question		Response
<b>Section 2: Setting and reviewing the electricity emissions target</b>	The Government's proposed approach to setting the initial electricity emissions targets under the Guarantee.	BlueScope supports the Government's approach in aligning the policy with Australia's commitment under the Paris Agreement and setting the target for the electricity sector in line with a 26 per cent reduction on 2005 levels by 2030.
	The Government's proposed approach to amending targets and setting future targets under the Guarantee:  One option is for the Government to take account of variations in demand when the next set of electricity emissions targets are set by 2025.	BlueScope acknowledges the need to reduce the uncertainty created by regular changes to emissions targets. However, the materiality of the inaccuracy and impact on the cost of the scheme to customers must be considered. Only reviewing targets every 5 years may not allow this consideration. It may be advantageous for the government to set 5 year rolling targets to provide 5 years of certainty at any point in time but also provide flexibility to adjust 5 years of targets between 5-10 years on an annual basis. This will provide certainty in always having targets

Question		Response
		locked in for 5 years with the flexibility and foresight beyond 5 years should any adjustments be required due to variations in demand and market conditions.
<b>Section 3:</b> <b>Implementing the exemption for EITE activities</b>	Whether the proposed approach to streamline the RET and Guarantee exemption applications minimises any regulatory burden for EITE entities.	<p>BlueScope believes that by retaining the CER as the regulator responsible for EITE exemptions, inconsistencies in the processes for exemption calculations should be avoided and the regulatory burden for applying for exemptions should be minimised. Given the proposal to utilise the same 'electricity use method' for calculating exemptions for EITE activities under both the RET and the Guarantee, BlueScope would see significant opportunity for the CER to streamline and minimise administrative requirements for applying for and processing exemptions.</p> <p>As such BlueScope is supportive of the approach being proposed by the Government to streamline the RET and Guarantee exemption application processes.</p>
<b>Section 4:</b> <b>External Offsets</b>	Whether market customers should be able to use offsets to reduce part of their emissions under the Guarantee.	<p>As described by the Energy Security Board, the Guarantee is a way to "encourage new investment in clean and low emissions technologies while allowing the electricity system to continue to operate reliably". The use of offsets to meet emissions requirement targets will reduce the overall contribution by the electricity sector to Australia's emissions reduction efforts and so access to offsets should only be considered at a level where they do not reduce or delay investment in reliable lower emissions generation technology. A failure to ensure the necessary investment in new generation (and eventual replacement of aging assets) will create tight market conditions and result in a high cost and increased reliability risk to consumers. A balance in the ability to use offsets for emissions requirement compliance purposes is therefore required to ensure the Guarantee's objectives are met, but at least cost.</p> <p>BlueScope supports the conditional use of offsets for the purposes of minimising the cost of abatement.</p>
	The proposed approach to using offsets to be used for compliance under the Guarantee.	<p>BlueScope supports market participants having access to both domestic and international offsets as a means of minimising the cost of abatement.</p> <p>Any cap and allocation of that cap should take into consideration the following high level considerations:</p> <ul style="list-style-type: none"> <li>• The expected impact on reducing investment and the emissions reduction activities carried out by the electricity sector</li> <li>• Its impact on competition. Is there a need to aid smaller participants by allocating a cap equally or does the 50 GWh exemption proposed by the ESB effectively deal with this issue?</li> <li>• The impact on the cost of carbon abatement to the overall economy- with tightening of baselines under the Safeguard Mechanism, the Guarantee may cause abatement costs to increase if the market cannot support the level of demand created by both policies.</li> </ul> <p>BlueScope also supports the Government's recognition that quality and additionality are also important in ensuring that abatement is credible and not double-counted.</p>

## Reliability Requirement

### Forecasting and updating the reliability requirement

The forecasting of the reliability gap is rightly recognised by the ESB as being fundamental to the success of the Guarantee. Providing enough information so that the forecasts can be reproduced and verified by an independent body is of high importance as this will provide a higher level of confidence for all stakeholders and also allow stakeholders the opportunity to be proactive by running scenarios and formulating compliance strategies ahead of any impending trigger. Reporting on forecast accuracy and assessing the forecast to best practice guidelines are also important in setting up the Guarantee for success.

BlueScope supports the measures outlined by the ESB to ensure forecast accuracy, transparency and reproducibility.

The identification of the timing of a gap in reliability as per the forecast must be as granular as possible otherwise the reliability requirement may impose unnecessary costs on customers. For example, if a gap year was identified and compliance was required for the year, the cost of compliance would be significant as compared to if a gap month was identified and compliance was required for only that month.

Under the current market structure, the most liquidity exists in quarterly products, therefore it would seem logical to forecast the reliability gap in quarters. However, working within the constraints of currently available contract structures could reduce opportunities for product innovation and lower cost compliance. It may be more advantageous to build a policy design to allow for the gap forecast period to be granular (e.g. monthly, daily, hourly) to support product innovation and flexibility in compliance options.

This granularity should also be reflected in assigning a liable entity's share of peak demand for the purposes of compliance under the Guarantee. This will ensure that customers with seasonal demand that do not contribute to a peak during the forecast gap period are not unfairly burdened with a costly obligation.

BlueScope would urge the ESB not to limit options for compliance or compliance at lowest cost by limiting the design to what is currently available in the contract market.

### Triggering the reliability requirement

As per the above discussion pertaining to the granularity of the forecast gap period, the triggers for T-3 and T-1 should align directly with the period of the gap. If the gap is forecast for 8 January 2025, the T-3 trigger should be 8 January 2022 and the T-1 trigger should be 8 January 2024. This will ensure that the period between T-3, T-1 and T is never greater than 3 years or 1 year respectively. This will allow maximum time for the market to react prior to enacting the trigger.

### Liable Entities

BlueScope strongly opposes large energy users becoming liable entities under the reliability requirement. The policy position is prefaced on the assumption that large energy users are better placed to manage the risk at a lower cost than retailers.

Contrary to this, the majority of large users are not market participants and do not have the capability to manage the obligation. Managing this obligation may incur significant cost in building capability for a trigger event that may not happen. Retailers already have this capability and are experienced at managing positions to cover C&I load. This is their business.

Furthermore, as presented by Brian Morris from Schneider Electric Australia at the Guarantee public forum, peak demand managed by individual customers may be significantly higher than a coincident demand managed by a retailer as a portfolio. Schneider's analysis showed that the sum of the individual peak demands of 36 of their customer sites was 360MW but the maximum demand of the portfolio, due to the non-coincident peaks, was 240MW. In this instance, the retailer would be required to enter into contracts for 33 per cent less demand than if managed by individual customers.

With respect to a threshold of 5MW, capturing approximately 100 NMI and 20 per cent of load, this threshold is very low. A 5MW customer is unlikely to be sophisticated enough or well enough resourced to understand and manage this obligation. They will need to rely on the expertise of retailers to do this. With no mandatory obligation for the retailer to accept a transfer of obligation, this policy position may reduce customer leverage and cause asymmetry in bargaining power and result in having to accept higher costs.

Responsibility for the reliability requirement in respect of non-market C&I customers should lie by default with retailers. However, BlueScope proposes that all energy users be given the flexibility to opt-in and manage this obligation themselves, if they choose to do so. This approach has worked well in other areas such as meeting obligations under the RET and is much better aligned to serving the interests of customers.

This flexibility will also need to be echoed in the provisions for managing contract positions in the event of a material change to a liable entities load between T-1 and T. The ESB has considered the circumstances in which a retailer may need to change their position however there is no detail or consideration of allowable adjustments for large users' contract positions if they manage the obligation themselves.

### Qualifying contracts

BlueScope welcomes the recognition by the ESB that contracts entered into prior to the Guarantee should be grandfathered and deemed firm under the reliability requirement. However, we believe that the proposed cut-off date of 20 April 2018 for the grandfathering provision does not recognise the significant time it takes to finalise a procurement strategy and enter into any power purchase agreement, whether it be a standard retail agreement or a more complex longer-term power purchase agreement.

We understand that the cut-off date is intended to prevent market participants from gaming this provision but we do not believe that a cut-off date prior to the grandfathering provisions being detailed is reasonable. Given the lack of information available on this provision up until the time of releasing the detailed design and the uncertainty in the COAG approval process, BlueScope proposes the cut-off date for contracts to qualify under the grandfathering provision should be the date that the detailed design is presented at the COAG Energy Ministers' Meeting in August.

BlueScope is also pleased to see the ESB taking steps to directly address stakeholder feedback on improving competition in the electricity market by proposing the Market Liquidity Obligation (MLO). This measure should improve liquidity and support price discovery.

We note that it is proposed that only flat and peak swaps are included in the MLO as there are concerns around the ability of generators to defend caps in a 5-minute settlement market. This is again limiting the design to products currently available, potentially limiting the efficiency of the market to maintain reliability at lowest cost. BlueScope suggests that the ESB review this decision with the view of incentivising development of new cap products (e.g. a cap that only pays if the P50 demand is exceeded and as such should be much easier to defend). Cap products are much more suitable than swaps to manage exposure to incidental increases in demand and allow market customers to avoid consistently over-hedging to cover such incidental increases. Considering this, it is important to have liquidity in cap products to ensure the obligation can be met at least cost.

With respect to providing an optimal outcome for customers, BlueScope supports the option of combining the MLO with a trade repository (with reporting). Daily reporting via a trade repository will improve liquidity by providing transparency and aiding in price formation. It will also strengthen the MLO by providing visibility of vertically integrated retailer internal transfers as these provide a reference for the rest of the market. If cost is prohibitive or burdensome for smaller participants, an exemption may be appropriate for these participants. This should not detract from the value of the repository as the majority of trading should still be captured. Where an entity is required to comply with the MLO and they are left with unwanted positions, we believe that this indicates uncompetitive pricing that needs to be addressed to clear the position and that it is not a cost imposed by being required to provide liquidity under the MLO.

### Voluntary Book Build

BlueScope supports the proposal for AEMO to administer a voluntary book build commencing at the T-3 trigger. A book build provides additional flexibility to manage the reliability obligation and it will also support transparency and price discovery. In addition, it can help to restrain market power in a tight market by providing a low-cost avenue to canvass interest for developers of new dispatchable capacity. The book-build approach could be aided by government support for new independent projects as proposed by the ACCC in their final report to their Retail Electricity Price Enquiry.

### Demand response contracts

BlueScope supports the use of demand response contracts as a means of compliance under the reliability requirement.

Implementing a transparent demand side response mechanism will allow the efficient utilisation of user controlled demand response and in turn help reduce peak load, volatility and high prices. Given that this is also an important tool in meeting the reliability requirement of the Guarantee, work on developing a mechanism (as part of the AEMC's Reliability Frameworks Review) should be given priority by the ESB and AEMC.

Thank you for the opportunity to provide feedback on the draft detailed design of the Guarantee. If further comment or clarification is required please contact Bridgette Carter, Manager Energy Sourcing & Utilisation on 02 4240 1749 or David Jenkins, Manager Government Relations on 03 9666 4022.

BlueScope looks forward to continuing discussions as the design and legislation are developed over the coming months.

Yours sincerely



**Mark Vassella**  
MANAGING DIRECTOR AND CEO