

13 July 2018

Dr Kerry Schott
Independent Chair
Energy Security Board

Submitted by email: info@esb.org.au

Dear Dr Schott,

ENERGY SECURITY BOARD NATIONAL ENERGY GUARANTEE DRAFT DETAILED DESIGN CONSULTATION PAPER

The Clean Energy Council (CEC) is the peak body for the clean energy industry in Australia. We represent and work with hundreds of leading businesses operating in solar, wind, hydro, bioenergy, marine, geothermal and energy storage along with more than 5,000 solar and battery installers. We are committed to accelerating the transformation of Australia's energy system to one that is smarter and cleaner.

The CEC appreciates the opportunity to respond to the Energy Security Board's (ESB's) National Energy Guarantee (NEG) Draft Detailed Design Consultation Paper and accompanying Technical Working Papers (herein referred to as 'the papers'). We support the intent of the NEG to integrate energy and emissions policy in a way that can overcome the continued politicisation of energy policy in Australia. We strongly believe that providing long-term policy certainty is vital to ensuring market confidence and encouraging investment in low emissions technologies that will ultimately bring down electricity prices.

The renewable energy industry is disappointed with the Commonwealth's proposal to adopt a 26 per cent emissions abatement target for the energy sector under the NEG. This target will deliver little or no new investment from the NEG and leaves responsibility for the energy transition to states and territories and energy customers. The energy sector can and should deliver a greater contribution to Australia's emissions abatement target given the availability of low cost abatement in the energy sector, particularly relative to other sectors of the economy such as transport and agriculture.

This submission focuses solely on the NEG design as outlined in the papers. Should the COAG Energy Council agree to progress with the NEG at its August meeting, the CEC wants to ensure a robust architecture that can be practically implemented and would be workable under a higher abatement target in the future.

The CEC welcomes the ESB's commitment to developing the NEG design in a consultative and cooperative way in a very limited timeframe. The ESB has made good progress on the architecture to date. The papers clearly reflect on the significant amount

of feedback received through the ESB's consultation process held earlier this year, technical working groups and one-on-one sessions with the CEC and other stakeholders. Should the COAG Energy Council agree to progress with the NEG, more work would still be required to clarify a number of practical details and broader consideration would need to be given to potential unintended consequences.

In our view, there have been two significant but valuable developments from the earlier NEG concept. First, the CEC welcomes the ESB's endeavours to ensure that the contracting approach to meet compliance under the NEG is flexible. This is most evident from the approach to registry allocations under the emissions reduction requirement as well as the technology neutral nature of and less prescriptive framework for determining qualifying contracts under the reliability requirement. Allowing flexible compliance options should assist to minimise the costs of complying with the mechanism and therefore, the costs to electricity consumers.

Second, we welcome the ESB's efforts to address competition and market power concerns under both the emissions reduction requirement and reliability requirement. The CEC notes there are recommendations in the Australian Competition and Consumer Commission's (ACCC's) recently released final report into retail electricity pricing that could have relevance to the NEG design. The CEC suggests the ESB prepare advice on the NEG competition measures and the recommendations made in the ACCC's report so that stakeholders can get a better understanding of the interplay between the two sets of competition measures.

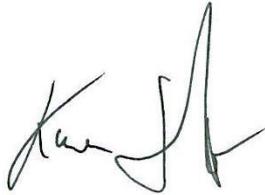
Should the COAG Energy Council agree to progress with the NEG, a vital next step would be the preparation of the legislative changes to give effect to the NEG. Clarity is required on what NEG elements would be in the National Electricity Law (NEL) versus National Electricity Rules (NER) as these two instruments operate in different ways. It is our view that the NEL should solely give effect to the NEG and the detail of the mechanism should be contained in the NER as this gives certainty that the policy will last and means changes to the mechanism will follow the well-understood, consultative rule making approach undertaken by the Australian Energy Market Commission.

We understand the ESB has been tasked with providing advice to the next COAG Energy Council meeting on how Western Australia might be able to participate in the emissions reduction requirement of the NEG. The CEC strongly believes that the NEG should be extended to cover both Western Australia and the Northern Territory given both have material emissions footprints for the electricity sector and the NEG offers a mechanism to address these.

The attachment to this submission provides commentary on specific design elements that the CEC considers require further attention by the ESB to ensure the effectiveness of the NEG architecture.

Thank you for the opportunity to contribute to the development of the NEG. Please contact Lillian Patterson, Director Energy Transformation, on 03 9929 4142 or at lpatterson@cleanenergycouncil.org.au for any queries regarding this submission.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Kane Thornton', with a stylized flourish at the end.

Kane Thornton
Chief Executive Officer

Emissions reduction requirement

Consultation paper reference	Clean Energy Council comments
3.3.2	<p>Residual unallocated generation</p> <p>The papers state that market customers that do not have generation output allocated for any part of their load by the end of the reporting period will be assigned the emissions intensity of the residual unallocated generation. The residual emission intensity will be floating with regular updates based on the emission intensity of unallocated generation.</p> <p>The CEC suggests that unallocated load should be automatically assigned the highest emissions intensity of all generation in the registry, which would be known at the start of each financial year. This provides a stronger signal for new investment in low emissions technology, which is one of the key objectives of the NEG. It should also drive liquidity as it provides a stronger incentive to contract with lower emissions intensity generation so that only the highest emission intensity generation ends up unallocated. Finally, it will assist market customers to better manage their positions as it reduces the risk of sudden, unexpected and potentially significant increases in the emissions intensity of the residual unallocated generation as generation is allocated in the registry, particularly in the lead up to the compliance date.</p>
3.3.3	<p>Pre-1997 generation</p> <p>The CEC considers all renewable generation, including those built before 1997, should be included in the emissions reduction requirement. Pre-1997 generators were provided a baseline under the Renewable Energy Target (RET) in order to deliver on the policy objective of driving additional renewable energy. The NEG as proposed does not have such a policy objective and therefore exclusion or adoption of baselines for pre-1997 (or any generation source for that matter) is inconsistent with the policy objectives of the NEG. Excluding or adopting baselines for pre-1997 technology would arbitrarily limit the contribution of pre-existing hydro power and therefore be distinctly in contradiction to the technology neutral intent of the policy, while adding undue complexity to an already complex policy architecture.</p>
3.3.3	<p>Non-market embedded generation</p> <p>The CEC agrees that non-market embedded generation that is non-renewable, over 5 MW and has an emissions threshold of 25,000 tCO₂-e should be included in the emissions reduction requirement. This avoids capturing back-up plant that rarely runs while still capturing generators that are off market but are high emitters.</p>

Consultation paper reference	Clean Energy Council comments
	<p>For non-market embedded generation that is renewable, we suggest these should be included on an opt-in basis to allow them the choice to participate in and receive potential benefits from the NEG.</p>
3.3.3	<p>Small-scale solar PV</p> <p>The CEC disagrees that the net exports from all small-scale solar PV installations should be added to the relevant retailer's load and automatically allocated to the retailer as zero emissions generation. The owners of rooftop solar systems have made their own substantial capital outlay for these systems and so should be given the choice as to how the emissions abatement from their systems are allocated. By allowing customers to opt-in, we believe this would incentivise retailer innovation and competition as retailers would look to develop new products that reward customers in return for their zero emissions generation.</p> <p>Potential arguments that the owners of small-scale solar PV already benefit from small-scale technology certificates (STCs) and feed-in tariffs (FiTs) are not strong:</p> <ul style="list-style-type: none"> • the STC deeming period decreases each year to 2030 so the benefit is continually reducing and will soon have no value; and • minimum FiTs are not legislated across all states and territories and FiTs are constantly changing as evidenced by the recent decision in NSW to reduce the state's feed-in tariff benchmark from 11.9-15c/kWh in 2016/17 to between 6.9-8.4c/kWh for 2018/19. <p>The CEC believes the practicalities of how this opt-in mechanism could be administered and accounted for in the registry could be easily worked out.</p>
3.3.3	<p>GreenPower</p> <p>The CEC continues to strongly support business and household consumers undertaking voluntary action to reduce emissions associated with their electricity use and that these should be additional to the NEG's emissions reduction requirement. We support the GreenPower program being additional to the emissions reduction requirement and the ESB working with the National GreenPower Steering Group to find a way to achieve this.</p> <p>The CEC recommends a clear mechanism be built into the emissions reduction requirement to further support additional voluntary actions by businesses and households. These customers should be able to undertake additional emissions reduction action within the energy sector and choose to voluntarily surrender this abatement outside of the GreenPower program.</p>

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	<p>In addition, while the GreenPower program is not legislated through the RET, the program's currency relies on the use of large-scale generation certificates (LGCs) under the RET, which is due to cease in 2030. This further supports the need for a separate mechanism for voluntary abatement in the NEG design.</p> <p>We believe developing such a mechanism would not add significant complexity to the registry balancing process given this can be achieved for larger issues such as the treatment of exempt emissions-intensive trade-exposed load.</p>
3.3.4	<p>Registry operations</p> <p><i>Developing the registry</i></p> <p>As the central infrastructure for the emissions reduction requirement, ensuring a registry that is transparent, flexible, easy to use and displays valuable information to facilitate efficient compliance is crucial. This requires that the Australian Energy Market Operator (AEMO) as the registry administrator engage with generators and market customers on its development in addition to the Australian Energy Regulator (AER), which is suggested in the papers.</p> <p><i>Information on the registry</i></p> <p>The registry development process will need to consider how best to balance transparency with the need to protect commercially sensitive information. The registry's sole function is as a compliance tool so it needs to disclose sufficient information to allow registry users to fulfil their compliance needs, such as the emissions intensity of each generator. While disaggregated information on generator or market customer positions may be necessary for the AER to assess compliance, it is not necessary that this information is revealed to registry users in order for them to fulfil their compliance obligations. In addition, the CEC does not support the papers' suggestion that the registry will disclose each generator's unallocated generation, nor do we support the disclosure of what generation has been allocated to which market customers. We consider both of these would reveal commercially sensitive information and could distort bargaining positions when negotiating contracts.</p> <p>In terms of aggregated information on scheme compliance, we agree with the papers' suggestion that the outcomes of each compliance year, including overall scheme outcomes, and the emissions intensity of each market customer should be published publicly in the year following the compliance year. This information should also include identifying which market customers have or have not been compliant with the emissions reduction requirement.</p>

Consultation paper reference	Clean Energy Council comments
	<p data-bbox="496 394 847 427"><i>User access to the registry</i></p> <p data-bbox="496 461 1406 797">The NEG design supports the development of secondary markets for emissions. The registry will need to be sufficiently flexible to ensure market customers can modify their position easily and allow counterparties to such trades, such as two market customers, to confirm a reallocation without the need for generator involvement. The ESB should also consider the need for intermediaries to access and actively participate in the registry. Intermediaries may facilitate trades between two counterparties where the counterparties are not revealed to one another. In such circumstances, the intermediary should be able to complete the allocations within the registry.</p> <p data-bbox="496 831 1406 1267">Similarly, the ESB should give further consideration to the role of intermediaries or agents on the generation side within the emissions registry. The owners of some generators may have contractual arrangements in place, such as power purchase agreements, where a gentailer undertakes market operations, such as bidding, on their behalf as an intermediary or agent. For the purposes of the NER, AEMO can interpret that the intermediary or agent is the generator given their control of market operations. As part of this arrangement, however, the owner retains the environmental rights to the generation. For example, the owner may not be providing the LGCs to the intermediary or agent under the current RET arrangements nor would they intend that the intermediary or agent is the controlling party to undertake allocations in the emissions registry.</p> <p data-bbox="496 1301 1406 1603">If the NEG applies the NER definition of generator then by virtue of the existing intermediary arrangements, the gentailer will become the default generator in the eyes of AEMO. The current NEG concept is clear that the generator is in control of emissions allocations from the facility for the purposes of the emissions registry. This combination results in a perverse outcome where the gentailer is in control of the emissions allocations of the entire facility and therefore could allocate the low emissions benefits to whoever it chooses (including itself) with no right of intervention from the facility's owner.</p> <p data-bbox="496 1637 1406 1839">The registry operations should facilitate this type of arrangement so that generation owners can undertake the emissions allocation in the registry and thus access the potential benefits associated with the NEG while still allowing intermediaries or agents to undertake market operations on their behalf if that is intended by their contractual agreement.</p> <p data-bbox="496 1872 863 1906"><i>Public access to the registry</i></p> <p data-bbox="496 1939 1406 2063">The papers state only market customers and generators will have access to the registry. This is justified on the basis that allowing access to third parties could create a risk that third parties may have generator output allocated to them at the reporting deadline. The CEC does not</p>

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	<p>consider this a valid reason to limit access to the registry. It should be simple to set up a restricted category for third parties who only intend to view the registry that removes any ability for generation to be allocated to them.</p> <p>There are additional reasons why a higher level of public transparency of the registry is justified. A transparent registry is vital for both new generators and market customers considering entering the market in order that they can get an understanding of and have confidence in its operations. In addition, allowing registry data to be publicly accessible is vital to public trust and therefore the durability of the NEG policy. We note that high levels of transparency in the REC registry have set a precedent of what stakeholders expect is reasonable and achievable. If the NEG does not provide a similar level of transparency, key stakeholders may become suspicious about the integrity and effectiveness of the policy.</p>
3.4.1	<p>Carrying forward over-achievement</p> <p>The CEC does not support a 5 per cent limit on the level of carry forward each year by market customers in addition to a fixed amount of 60,000 tCO₂-e. Placing such a low limit on banking may act as a barrier to cost effective and long-term investment in low emissions generation. A materially higher limit supports logical commercial transactions by providing an incentive to invest earlier to meet the emission target and allowing investors in new low emissions capacity to realise the full capacity of the emission reductions they achieve.</p> <p>The CEC would not expect an unlimited ability to carry forward over-achievement, but we consider a limit between 20 and 30 per cent would more effectively preserve the signal to invest while mitigating the risk of anti-competitive stockpiling.</p>
3.4.2	<p>Deferring compliance</p> <p>Tight controls on the ability to defer compliance are necessary to ensure strong incentives for liable entities to support new investment in low emissions generation that is critical to delivering on the objectives of the NEG. The papers suggest it may be appropriate to start the scheme with a greater proportional deferral limit that becomes smaller over time. However, the papers suggest the 10 per cent limit will be set from the outset and this could be amended through future rule changes.</p> <p>The CEC proposes that this winding down of the limit should be outlined in the NER from the outset and not updated through rule-change processes in the future as is proposed. The 10 per cent limit on borrowing may be appropriate when the NEG commences but the progressive step down in the limit should also be clearly defined to provide certainty to the market.</p>

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3.4.3	<p>Use of offsets</p> <p>As detailed in our submission to the Commonwealth’s draft detailed design consultation paper, the CEC is strongly opposed to the inclusion of external offsets to meet the emissions requirement. Offsets will simply result in liable parties deferring commitments that support new investment in generation, resulting in less new energy supply and therefore, higher wholesale and retail energy prices.</p> <p>The inclusion of offsets is in stark contrast to the very objectives of the NEG to ensure reliability, affordability and environmental sustainability of Australia’s electricity system.</p>
3.5.4	<p>Enforcement tools for the emissions reduction requirement</p> <p>The CEC supports a culture of compliance as important to ensuring market customers comply with the emissions reduction requirement. Compliance should be encouraged through informing, educating and encouraging stakeholders to avoid the need for enforcement action after a breach has occurred. We support the AER taking an active role in engaging with and educating the market to ensure participants understand their obligations and are encouraged to comply with the requirement. Annual reporting of compliance is key to this process.</p> <p>However, in cases of non-compliance, the CEC would prefer a clearer and more rigorous approach than the proposed AER discretion to pursue a range of enforcement options (i.e. civil proceedings, administrative undertakings, infringement notices or court enforceable undertakings). We would prefer to see a clearly defined penalty price for non-compliance with the emissions reduction requirement. A penalty price is a more effective enforcement tool as it would send a strong signal to the market of the cost risk associated with non-compliance.</p>

Reliability requirement

Consultation paper reference	Clean Energy Council comments
4.2	<p>Forecasting the reliability requirement</p> <p>The effectiveness of the NEG to incentivise retailers and large customers to support the reliability of the power system through their contracting and investment in resources is highly dependent on the accuracy of forecasts. Stakeholders need to have confidence in the robustness and reliability of the forecasting methodology. The papers rightly suggest that AEMO will be required to consult with stakeholders through a formal consultation process during the development of forecasts leading up to the Electricity Statement of Opportunities (ESOO) publication and then after the ESOO has been published to review the forecasting process and results.</p> <p>The papers suggest this consultation should occur through an expanded Forecasting Reference Group (FRG). The CEC cautions that this may not be the most effective means to engage stakeholders. The FRG conducts monthly meetings covering all aspects of gas and electricity forecasting and market modelling. Participants with an interest in the forecasting for the reliability requirement may not be actively engaged in a forum that meets so regularly and on a wide range of different matters.</p> <p>The ESB should give further consideration to how AEMO can better engage with stakeholders. If the FRG is still considered the most appropriate forum for these discussions, there should at least be wider notices to alert interested stakeholders to participate in the specific meetings addressing forecasting for the reliability requirement. This system to notify interested stakeholders could also be used for the consultation on AEMO's annual improvement program to ensure that assumptions and modelling approaches are tested and transparent.</p>
4.4	<p>Triggering the reliability obligation</p> <p>There is still a significant amount of detail that needs to be developed around the assessment to determine that a reliability gap is material. The CEC supports the proposal for the NER to set out a transparent framework to allow AEMO to determine this materiality and the details will be outlined in an AEMO guideline.</p> <p>Defining materiality is important to ensure that the reliability obligation is triggered only when necessary. The CEC suggests there should also be a mechanism to 'untrigger' the reliability obligation should further forecast revisions indicate a change in the reliability gap such that no material gap persists. It is feasible that due to changing market fundamentals, particularly those outside of the control of liable entities, a reliability gap could reduce to no longer be material or even close completely following the triggering of the reliability obligation. In such</p>

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	a situation, the reliability obligation should be removed and compliance should not be assessed.
4.5	<p>Liable entities</p> <p>The CEC seeks clarity on the treatment of storage (large-scale batteries and pumped hydro) under the reliability requirement. As both a generator and load, storage could be considered a liable entity as they could be captured by the definition of large customers with a load above a threshold of 5 MW peak demand. As a result, storage would need to comply by entering into qualifying contracts should the reliability obligation be triggered. It would be a perverse outcome if investment in energy storage were to be disincentivised due to the reliability obligation given the substantial contribution energy storage can make towards the reliability of the energy system. The policy intent of the NEG is to incentivise these types of facilities and so requiring them to comply would be contrary to this intent.</p> <p>We suggest that scheduled loads, which are a subset of the market customer participant category, should be exempt from the reliability obligation. By definition, loads that can be scheduled do not contribute to peak demand as they are managed by AEMO. Clarifying this in the NER will strengthen the incentive to invest in large-scale batteries and pumped hydro to support the reliability of the power system.</p>
4.6	<p>Qualifying contracts</p> <p>The proposed framework to provide flexibility to liable entities to purchase a range of products to meet their compliance obligations if the reliability obligation is triggered is a welcome development. The CEC suggests the ESB continue to consult with stakeholders to ensure the market clearly understands how contracts will be treated under the reliability requirement. In particular, this should include further work on the firmness factor to be applied to contracts. We suggest that while it may be appropriate that liable entities have discretion about how they determine the firmness factor of their contracts, some guidance on what should be included in the firmness factor methodology is still necessary.</p>
4.8	<p>Compliance</p> <p>Given one of the criteria for the AER to assess compliance is if AEMO has procured additional resources through the Reliability and Reserve Trader (RERT) framework, the CEC urges that more transparency and accountability is required around how AEMO procures and activates RERT. This is particularly pertinent given AEMO's proposed enhanced RERT rule change suggests significant changes to the current RERT arrangements, such as availability payments, three-year contracts and minimum budgets. These changes could significantly increase the</p>

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	costs associated with RERT. This is important for the NEG to ensure a compliance and penalties framework that is fair and transparent.
4.9	<p>Penalties</p> <p>The CEC agrees that charging a liable entity found to be non-compliant with the reliability obligation a predetermined proportionate cost per MW of non-compliance makes it very clear to liable entities that non-compliance has a clear cost risk. We caution, however, that basing this on a multiplier of the capacity cost of new capacity is complicated. The example given in the papers refers to the capital cost of diesel generation. However, the reserves procured through AEMO's Procurer of Last Resort function could be diesel generation, demand response or something else. Further consideration should be given to this.</p>