Dr Kerry Schott AO
Energy Security Board
Email: info@esb.org.au

Friday, 05 April 2019

Dear Dr Schott,

Retailer Reliability Obligation, Draft Rules Consultation Paper

ENGIE in Australia (ENGIE) welcomes the opportunity to make a submission in response to the Energy Security Board's (ESB) abovementioned consultation paper. ENGIE commends the ESB for its efforts to engage with industry in the development of the Retailer Reliability Obligation (RRO) (especially given the timeframes proposed for introduction).

ENGIE is a global energy operator in the businesses of electricity, natural gas and energy services. In Australia, ENGIE has interests in generation, renewable energy development, and energy services. ENGIE also owns Simply Energy which provides electricity and gas to more than 680,000 retail customer accounts across Victoria, South Australia, New South Wales and Queensland.

ENGIE remains concerned that the overarching drivers of the RRO do not justify the interventions proposed but appreciates that this matter of policy has been settled. As such, this submission focuses on relevant implementation issues.

Discussion

Reliability forecast and Reliability Instrument

In broad terms, ENGIE is comfortable with:

- the mechanism for making a reliability forecast;
- the process for updating a reliability forecast; and
- the triggering of a reliability obligation.

Nonetheless, ENGIE suggests that where there are valid concerns about the forecasts made by the Australian Energy Market Operator (AEMO) there may not be sufficient scope to prevent a Reliability Instrument being made. While ENGIE believes AEMO will approach its role professionally, an element of conservatism will likely encourage a wide gap period be announced as not. In such circumstances, it is not unreasonable to expect the Australian Energy Regulator (AER) to undertake a detailed merits review as opposed to a limited administrative review prior to approving the issuance of a Reliability Instrument.

ENGIE is a member of the Australian Energy Council (AEC), and for much the same reason as above, agrees with the AEC's position that the AER's issuance of a Reliability Instrument should be based on a material breach of the Reliability Standard not a "trivial" breach. This will have two benefits: (1) it will reduce compliance costs that would otherwise arise when a minor breach occurs; and (2) it will better encourage AEMO to ensure its forecasts more accurately reflect the significance of a potential breach. It would be a poor outcome if the RRO is triggered for multiple but limited breaches which ultimately do not require action in the market or justify the RRO obligations. In fact, it may be quite easy to make a case for limited breaches three years in advance across rolling years which may ultimately not justify action.

Market Liquidity Obligation

ENGIE remains disappointed that detailed and significant points raised with the ESB and in the context of the *Market Making Arrangements in the NEM Rule Change* have not been adequately resolved. This includes the broad preference for a voluntary mechanism over compulsion.

Most concerning, the situation where a generator is unable to offer physical coverage for contracts that it is obligated to trade due to the Market Liquidity Obligation (MLO) means the ESB is supporting a policy position that may requires those generators to become financial speculators. This is an inappropriate position to place those companies in and is likely to be in direct conflict with company boards who are unwilling to permit speculative trading.

This outcome could arise in numerous circumstances.

- Where a gas fired generator is unable to procure additional fuel or there is a mismatch between financial hedges sold and running profile. The ESB has not addressed how gas-fired generators should be expected to rely on a gas market which is not dynamic and cannot guarantee delivery and receipt of fuel and transport to physically meet hedges that were sold under the MLO.
- A circumstance where a hydro facility was affected by drought or low water reserves may result in a similar inability to provide physical cover.

- Where a generator has fully contracted available capacity and / or financial capacity to a party in the market already either as an electricity contract or a structured deal.
- Where a generator elects to mothball units due to prevailing economic conditions during the MLO period – unless it should be assumed such capacity is withdrawn from the MLO.
- Where fuel costs exceed electricity market outcomes and thereby the participant will be forced to lock in unfavourable speculative positions.

While coal generators may be less likely to share these concerns, intermediate and peaking plant, and plant that are more likely to be fuel constrained may.

While ENGIE has concerns with the MLO that have not been addressed it does not believe the deeming approach proposed by the ESB is less appropriate under the circumstances.

ENGIE does have concerns regarding the bid and offer spread proposed by the ESB. In short, the MLO should be used to encourage market activity by framing the market. The tight spreads proposed by the ESB may inadvertently result in obligated and unwilling market makers being on one side of most trades. That should not be the purpose and would signal the failure of the MLO policy and point to more serious concerns with the market. A wider spread therefore would ensure that obligated and unwilling parties become an available last resort not the main counterparties in the market.

Thus, while ENGIE appreciates the ESB has undertaken a statistical analysis which shows historical spreads within 3 per cent, this does not translate to a conclusion that an appropriate market making spread should be limited to an upper bound of 3 per cent. ENGIE again encourages the ESB to be guided by the expertise of the Australian Stock Exchange in this space where they have a long history and detailed experience of making markets in Australia and in other jurisdictions across several industries.

Generator retirement

ENGIE does not believe new arrangements regarding notification should be amended because of the RRO. The issue of retirement notification has only recently been settled.

Opt-in customers

ENGIE is comfortable with the arrangements for opt-in customers; however, requires clarification that once a decision is made to opt-in this remains in place until the gap period has passed.

More broadly, ENGIE notes that “pool pass through” customers are not an insignificant part of the market and represent a certain form of energy provider business model. The ESB should be prepared for the impacts on these customers whose strategies have in effect been determined as not in the interests of the wider market.

ENGIE is not criticising the decision on treatment of these market customers per se but rather noting that this matter may not have been given due attention over the course of the development of the RRO.

Voluntary book build

ENGIE remains uncertain about the role of the voluntary book build. Nonetheless, the arrangements for the book build are relatively straight forward with the exception that ENGIE does not wish to be forced to contribute to AEMO cost recovery for undertaking the voluntary book build process. ENGIE has reached this view as it is aware that existing market participants already willingly perform these functions.

Conclusion

ENGIE once again appreciates the ESB's exemplary efforts to consult with a wide range of stakeholders and industry participants. The efforts of the ESB staff are commendable. Nonetheless, ENGIE encourages the ESB to consider the matters raised in this submission and clarify the rules as appropriate.

Should you wish to discuss any aspects of this submission, please do not hesitate to contact me on, telephone, 03 9617 8415.

Yours sincerely,

Jamie Lowe
Head of Regulation