



Our Ref: National Energy Guarantee
Direct Phone: (08) 8343 8154
Email: Jeff.olling@epic.com.au

8 March 2018

Dr Kerry Schott AO
Independent Chair
Energy Security Board

Submitted via email: info@esb.org.au

Submission to the Energy Security Board: National Energy Guarantee's 'Draft Design Consultation Paper'

Introduction

Epic Energy South Australia Pty Ltd (EESA) welcomes the opportunity to comment on the Energy Security Board's (ESB) National Energy Guarantee's 'Draft Design Consultation Paper' (the consultation paper), released on 15 February 2018.

EESA owns and operates more than 1,200 km of gas transmission pipelines in South Australia, including the Moomba to Adelaide Pipeline System (MAPS) and the South East Pipeline System (SEPS), which are uncovered (non-scheme) pipelines¹. Our customers include gas retailers, gas producers and industrial customers, many of whom use both the MAPS and the SEPS. Access to these pipelines is currently provided on a non-discriminatory, open access basis, with services designed to meet customers' needs in a cost-effective manner.

EESA welcomes an integrated climate and energy policy. Clear and stable policy settings, with bipartisan support, will create certainty for investors, increase competition, and theoretically, decrease costs to the end consumer.

In principle, EESA also supports both an emissions and reliability requirements, as proposed in the Energy Security Board's (ESB) proposed National Energy Guarantee (NEG).

¹ Coverage of the SEPS was revoked by the National Competition Council on 20 April 2000 and coverage of the MAPS was revoked on 30 September 2007.

Given the fact that South Australia has the highest renewable energy component in Australia (at nearly 50 percent of the state's energy mix, which is set to increase to 75 percent by 2025 under the current government), and the intermittent nature of renewables, the reliability of energy supply for South Australian's is imperative.

However, reliability of energy supply in South Australia hinges on its ability to deliver into the grid the appropriate level of dispatchable energy from sources which can quickly respond to short-term spikes in demand.

As recently as last month, the International Energy Agency noted that the increasing penetration of intermittent renewable energy into grids requires support from on-call energy sources, and in particular gas-fired generation, to maintain a reliable electricity grid².

Gas-fired generation generally, and fast start gas-fired generation facilities (which are capable of operating at full capacity within five minutes of start) in particular, already provide flexible, efficient and cost-effective synchronous generation capacity in response to the rapidly changing South Australian electricity market.

The introduction of a reliability requirement is a proactive and important step in the process.

At this preliminary stage in the design and development process, EESA has some general comments and/or concerns regarding the mechanics of the NEG, particularly in relation to the reliability requirement, as noted below.

(i) 'Reliable' generation

The NEG requires retailers to develop, or contract with generators for, a minimum level of 'dispatchable, on demand' (i.e reliable) electricity generation where there is an identified reliability gap. However, the consultation paper does not seem to define the types of generation that are considered 'dispatchable or reliable' under the NEG.

EESA considers that natural gas-fired generators' supply contracts should be captured as they are physically backed (unlike wind and solar), adding to their perceived reliability in terms of guaranteeing dispatchable capacity.

Again, the consultation paper does not discuss the logistics of how reliable capacity and the contracts will be logged by the regulator.

EESA looks forward to further detail and clarification around these points as the process continues.

(ii) 'Qualifying instruments'

Once the reliability gap is determined and allocated, retailers must demonstrate that they have sufficient 'qualifying instruments' to satisfy their share of the gap, in order to comply with their obligations under the NEG. EESA appreciates that the qualifying criteria must be sufficiently broad to anticipate a number of different contracting instruments presently employed under the National Electricity Market (NEM). However, as presently expressed,

² *Energy Policies of IEA Countries - Australia 2018 Review*: International Energy Agency, February 2018

what constitutes a 'qualifying instrument' could be argued as being complex, and at this stage of the process difficult to be implemented and work in practice.

EESA looks forward to further detail and consultation on this point as the process continues.

(iii) Interplay of legislative schemes

Understandably at this preliminary stage of development, there is little to no detail in the consultation paper regarding the integration of the NEG into the current National Electricity Law (NEL) and National Electricity Rules (NER), or the practical interplay of the regimes.

EESA looks forward to further detail and consultation on this point as the process continues.

(iv) Forecasting

Forecasting of the reliability gap has significant ramifications for the market and its participants in terms of investment signalling and obligations triggered under the reliability requirement, respectively.

The ESB has proposed in the consultation paper that the forecasting horizon for the purposes of the reliability requirement should be set somewhere between 2-3 and 10 years, with weekly or monthly updates for shorter forecast horizons and quarterly or annual updates for longer forecast horizons. It has also proposed short-term (3 months-1 year) or long-term (3-5 years) trigger points for the reliability requirement.

In light of the volatility of the South Australian electricity market and unpredictability in the current political environment, EESA considers that a medium-longer term forecast horizon and annual updates (in the absence of a material change in circumstances) may be appropriate. Similarly, EESA considers a 1-2 year trigger point may also be appropriate, to allow retailers and Australian Energy Market Operator (AEMO), sufficient lead times to respond. It would also guard against the development of short-term, inefficient strategies, and resultant increased prices for end consumers.

EESA does note however, that the allocation of a share of the reliability gap to a retailer years in advance is potentially problematic, with the potential for shortfalls in the event that the retailer is unable to complete its obligations at a later date, albeit due to financial difficulties or the closure/retirement of a contracted facility.

EESA will revisit its views in this regard as the design process continues over the coming months.

EESA further recommends that forecasting be independently tested to increase transparency and market confidence in the process.

(v) Methodology

The methodology for calculating dispatchable power under the NEG will be a key driver of the cost impact of the reliability requirement. Given the relatively low levels of dispatchable power available in South Australia, it is likely to have greater cost implications to the end consumer in this region.

EESA looks forward to further detail and consultation on this point as the process continues.

(vi) Interaction between the emissions and reliability requirements

At this preliminary stage of development, the consultation paper does not sufficiently explain how the emissions and reliability requirements are anticipated to work together.

EESA looks forward to further detail and consultation on this point as the process continues.

(vii) Compliance

At this preliminary stage of development, the consultation paper provides little detail on the reporting and other compliance obligations of market participants under the NEG. Such obligations should be carefully considered to avoid placing an unduly onerous burden on market participants and increasing costs to the system.

EESA looks forward to further detail and consultation on this point, to ensure a workable, cost-effective and efficient system for all participants.

(viii) Penalties

EESA supports a range of penalty options commensurate with the level of non-compliance. Generally, EESA considers the most appropriate penalty for non-compliance would be allocated costs. However, depending on the circumstances of non-compliance, it may be appropriate for a discretionary punitive 'penalty plus costs' penalty to be imposed. This may serve as a deterrent for non-compliance, but it must also be balanced against retailers factoring in the costs of potential penalties into their risk management strategies, which would likely be passed on to the end consumer.

Certain parameters should also be set around the Australian Energy Regulator's use of the discretion to ensure transparency, consistency and certainty for market participants.

EESA looks forward to further detail and consultation on this point as the process continues.

(ix) 'Book-build' option

The consultation paper raises an alternative for retailers to remedy the reliability gap, before the trigger takes effect, by bidding the new capacity at auction. This 'book-build' auction price may ultimately become the price setter (which may not necessarily reflect efficient pricing and costs, and which may in the long run be passed on to the end consumer).

EESA is mindful of competition and productivity impacts and looks forward to further clarification and consultation on the issue as the process continues.

(x) Administration

Given the complexity of the NEG, EESA looks forward to the further opportunities for consultation between government and industry in respect of the policies and procedures for the oversight of the NEG by regulators.

As one case in point, EESA recommends that regulators give due consideration to the implementation of sufficient mechanisms to prevent the disclosure of commercially sensitive information (pricing) to other market participants.

Concluding comments

EESA is encouraged that the NEG incentivises natural gas powered generation in South Australia. The NEG has the potential to provide new opportunities for natural gas, as a reliable and low-emissions transition fuel, and renewables, to partner in providing affordable, reliable and low-emissions energy to Australian consumers and industry.

Further, and irrespective of the final design the NEG takes, it is imperative that all state jurisdictions agree on the mechanics of the model, and that there be bipartisan support at both a state and federal level, for investment certainty. As such, the policy must have enough detail flexibility so when governments change, the NEG can still operate effectively under different policy settings.

EESA also looks forward to taking part in the ongoing consultation process for design and development of the model.

EESA confirms that this submission can be made publicly available.

Should you require further information regarding any of the comments made in this submission, please do not hesitate to contact Jeff Olling, Manager, Government, Regulatory and Stakeholder Relations on (08) 8343 8154 or by email: jeff.olling@epic.com.au.

Yours sincerely



Reynard Smith
General Manager, Strategy and Commercial