13 July 2018

Dr Kerry Schott AO
Independent Chair
Energy Security Board

Submitted by email: info@esb.org.au

Dear Dr Schott,

Origin response to Draft Detailed Design Consultation Paper

Origin Energy Limited (Origin) welcomes the opportunity to make a submission to the Energy Security Board's draft detailed design consultation paper for the proposed National Energy Guarantee.

Origin supports the objectives of the NEG to bring together energy and climate change policy and provide a clear investment signal for low emissions and reliable generation sources at least cost to Australian homes and businesses. With investment under the RET now largely met, policy direction beyond 2020 is critical to driving further investment, maintaining reliability and putting downward pressure on prices.

It is crucial that the NEG remain focused on achieving these three core objectives. We are concerned the NEG may become encumbered with unrelated measures such as calls for a generation fund or requirements for retailers to be market makers. The NEG should focus on its core objectives - conflation with other issues and subsequent interventions are likely to undermine investment signals and add costs and should be avoided.

Origin supports the international target to limit global warming to no more than 2°C and notes the strong intention of the Paris Agreement to pursue efforts to a 1.5°C scenario. We support Australia's announced 2030 target as a minimum goal for the nation and believe that greater ambition is possible over time. The electricity sector can do more than its pro rata share of the target as it has cost effective abatement options available to it which could be unlocked given the right policy settings.

This submission focuses on the following key points:

- ***Emissions obligation*** – the proposed emissions registry appears workable but we would support additional flexibility in the scheme including:
    - less restrictions on banking between years; and
    - a simpler approach to the allocation of load and generation in the registry which allows market signals to encourage the least cost approach.

- ***Reliability obligation*** - we view the proposed reliability obligation as a workable scheme that should support investment signals in reliable generation. We suggest that the proposed Market Liquidity Obligation be considered as a staged process and encourage the ESB to take time to further consult on this issue.

Origin Energy Limited ABN 30 000 051 696
www.originenergy.com.au

Emissions obligation

Origin has consistently advocated for more ambitious targets for the electricity sector. We support the Paris Agreement on climate change and support Australia's 2030 emissions reduction target as a starting point with greater ambition expected over time, consistent with the framework of the Agreement. We believe that the electricity sector can be responsible for more than its proportionate share of any national carbon reduction measure because it has viable options at scale to reduce emissions and can help unlock abatement in other sectors of the economy. Further, we believe an analysis of what abatement is expected of each sector of the economy is required, as has been recommended under the 2017 Review of Climate Change Policies.

Origin has committed to halving our emissions by 2032, which we will achieve by exiting coal, increasing our reliance on gas and growing renewables. We've already committed to 1,200 MW of new renewables since March 2016.

In the context of the NEG, Origin provides the following more specific comments on the emissions obligation:

- **Banking** - limits are proposed on the over-achievement of targets in a scheme year in an attempt to promote competition. This limit is suggested as 5% plus a nominal absolute amount of 60,000 tCO_2-e. Origin does not support limits on banking as it reduces flexibility and potentially increases compliance costs over a multi-year period. It may also act as a disincentive to invest in new low emissions generation. Previous schemes (LRET, carbon price) had no limit on banking as it is generally considered that banking allows liable parties to smooth costs over a period of time. Whilst Origin would prefer no limit on banking, a higher limit, say 20-30%, is suggested as a potential starting point. If this was included in the NEL Rules it could be modified over time by the normal AEMC Rule change process.

- **Emissions registry** – the proposed rules for the registry have changed significantly since the previous round of consultation. All generation will start as unallocated, with retailers and generators needing to contract for emissions over the course of the compliance year or risk having a residual intensity assigned to any unallocated load which may be deemed at a relatively high intensity. The current consultation paper has suggested that penalties will also apply if any load or generation is over-allocated in the registry. Whilst we understand the desire to create strong incentives for all parties to exactly allocate generation to load, we believe the previous draft design of the emissions registry provided a more elegant solution and should be preferred. That particular design relied on market signals for parties to allocate load and generation, with the strong incentive being provided by the potential application of the residual pool. This residual would likely have a very high emissions intensity and provided a clear incentive to contract. We would suggest there needs to be some flexibility to make use of this residual pool, without other specific penalty. This is particularly the case as the NEG is a new type of scheme design and is relatively complex.

- **Registry data publication** – we believe further consultation is required on exactly what information from the emissions registry should be made publicly available. This could take place during the development of detailed rules. Generally, we support aggregated information only to be made available. Information on individual generators (including any unallocated generation) should remain confidential.

- **Penalty price** – a traditional "penalty price" as used in the LRET is not proposed for the NEG. Instead, the AER will be used as the enforcement agency and may apply civil penalties of up to $100 million for breaches of the NEL. Origin would prefer a penalty price of some form be stated in the scheme rules that has some degree of proportionality between the breach and the penalty. This will aid in efficient compliance with the emissions obligation as it sets a known bound of prices and generally helps to achieve high levels of scheme compliance.

- **GreenPower and other voluntary products** - the NEG should be designed so that voluntary green schemes (such as GreenPower) remain additional and can continue to be offered to consumers. We support the intent of the ESB to ensure the additionality of such products and support further consultation on this issue. It is important that the additionality of voluntary offerings is maintained so that retailers can continue to offer new products as the market evolves.

Reliability obligation

We view the proposed reliability obligation as a workable scheme that should support investment signals in reliable generation. Essentially it puts the market on notice to invest or face potential penalties, with a safety net provided by the Reliability and Emergency Reserve Trader (RERT), which is familiar to market participants.

Our main comments on the proposed reliability obligation are as follows:

- **Qualifying contracts** – we support the broad approach of allowing various financial contracts to qualify as contributing to meet any reliability requirement. A broad range of instruments assists with promoting competition in the market and should enable a least cost approach.

- **Forecasting process** – we support the endeavour to continuously improve the forecasting process as the market progresses through a period of unprecedented change. We recognise that increased transparency around what causes unserved energy (USE) will go a long way to giving confidence in the results. This will ensure there is a clear understanding of the market's energy and reliability requirements, to help ensure a least cost outcome is achieved.

- **Independent review of any trigger period** – we support the proposal for an independent body, such as the AER, to be responsible for authorising a recommendation from AEMO to trigger the reliability obligation. This framework is a prudent governance structure and will provide additional confidence to the market.

- **Market liquidity obligation** – we agree it is important to ensure the NEG does not diminish market liquidity and competitiveness and we consider that the proposed approach in assessing qualifying contracts should address such concerns. Given this, we do not see the proposed Market Liquidity Obligation as contributing to the overall objectives of the reliability obligation and note that it runs the risk of added costs and market distortion. There is sufficient time for further consultation on this issue during the detailed Rules development phase and we suggest that the ESB consider how the proposal could be further refined. We believe that a staged approach to addressing this issue has merit, and could involve:

    - Market monitoring – the AER could monitor each region for any observed decline in market liquidity due to the NEG.
    - Voluntary phase – if an issue was shown by the AER market monitoring process then this could be communicated to the market which could be given the opportunity to increase liquidity in the region through voluntary actions. The period of time for any voluntary action could be limited and communicated up-front.

- Mandatory phase – only if there was no improvement in market liquidity during the voluntary phase would any mandatory obligations come into force. We suggest that any obligations be tailored to specific regions.

- **T-1 contracting position** – the high-level design indicated that the assessment of retailers' compliance with any reliability obligation would be considered ex post. We do not support proposals to view retailers contract positions one year out from any forecast shortfall event. The majority of retailers do not have their contracting position set one year out. If compliance is based against T-1 then we suggest that flexibility be built into any administrative requirements to notify the AER of changes to contract position in the period between T-1 and T.

- **Alternate design for the reliability obligation** – we understand that the South Australian Government has proposed an alternate design for the reliability obligation which would remove the notice given at T-3. Origin prefers the current design of the reliability obligation as described in the formal consultation paper and views the notice given at T-3 as of benefit. If the ESB believes that the alternate proposal has merit then we recommend that specific consultation be undertaken on this. It is difficult for market participants to give considered feedback on such a fundamental change to scheme design at this late stage in the process.

Other comments

- **Legislative implementation** – we seek further clarity on what design elements are proposed to be established in the National Electricity Law (NEL) and those that will be in the associated Rules. This is important as the Law and the Rules can be changed in different ways – the former by agreement through COAG Energy Council and the latter by AEMC Rule Change. Whilst the ESB is seeking to have a high-level scheme design approved by COAG Energy Council in August, there will be ongoing work over the second half of 2018 and into 2019 to develop the detailed Rules which underpin this scheme design. We encourage the ESB and Commonwealth government to continue to consult with industry during this process.

- **Pre-1997 generation** – we understand there have been some suggestions for legacy hydro assets to be excluded from earning a benefit under the emissions obligation. This appears to be based on similar arrangements in the LRET, which only allows legacy hydro to generate certificates if they are above historical baselines. However, the LRET is a different type of scheme as it encourages new renewable energy generation. The NEG emissions obligation is intended to cover all generation sources, old and new, and provide incentives to reach an overall NEM-wide emissions intensity. Therefore, we see no valid reason why legacy hydro should be excluded from gaining the full benefit of its low emission profile under the NEG.

- **Co-insurance for reliability obligation** – we also understand there has been some suggestions for a co-insurance scheme to mitigate risk for liable parties under the reliability obligation. We do not support a co-insurance approach as it creates moral hazard by potentially shifting risk from the parties best placed to manage it. It may also increase scheme costs for the market as a whole. We believe it should be left to individual liable parties to manage their exposure to the reliability obligation as they see fit.

If you wish to discuss any aspect of this submission further, please contact Matthew Kaspura at matthew.kaspura@originenergy.com.au or on 02 9503 5178.

Yours sincerely,

Keith Robertson
General Manager Regulatory Policy
Origin Energy Limited
GPO Box 5376
Sydney NSW 2001
+61 2 9503 5674–Keith.Robertson@originenergy.com.au