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Dr Kerry Schott AO

Chair, Energy Security Board

Submitted by email: info@esb.org.au

12 December 2018

Consultation on Retailer Reliability Obligation Impact Analysis

Dear Dr Schott,

AGL Energy (**AGL**) welcomes the opportunity to make a submission in response to the Energy Security Board's (**ESB**) Consultation on its Retailer Reliability Obligation Impact Analysis (**Impact Analysis**).

AGL is one of Australia's largest integrated energy companies and the largest ASX listed owner, operator and developer of renewable generation. Our diverse power generation portfolio includes base, peaking and intermediate generation plants, spread across traditional thermal generation as well as renewable sources. AGL is also a significant retailer of energy, providing energy solutions to around 3.5 million customers throughout eastern Australia.

In addition, AGL is continually innovating our suite of distributed energy services and solutions for customers of all sizes. These behind-the-meter energy solutions involve new and emerging technologies such as energy storage, electric vehicles, solar PV systems, digital meters, and home energy management services delivered through digital applications.

The role of the RRO

On 30 November 2018, the ESB, on behalf of the COAG Energy Council released its Impact Analysis of the proposed Retailer Reliability Obligation (**RRO**).

The Impact Analysis draws heavily from work undertaken by Frontier Economics and ACIL Allen Consulting to inform the final design of the National Energy Guarantee (**Guarantee**) that was provided to the COAG Energy Council in August 2018 (**Final Detailed Design**)¹.

In the ESB's Final Detailed Design for the Guarantee, ACIL Allen found that annual average residential retail electricity bills were projected to be around \$550 lower, on average, over the 2020-21 to 2029-30 period than in 2017-18 if the Guarantee was implemented. The modelling suggested that around \$400 of savings were as a result of BAU reductions in the wholesale price and \$150 of savings were due to the implementation of the Guarantee (**Guarantee Case**).

This figure built upon previous modelling by Frontier Economics in the Regulatory Impact Statement (**RIS**)² for the Guarantee, which found that the average bill saving from implementing the Guarantee, compared to the do-nothing scenario, would be around \$120 a year for the 2020 to 2030 period. This was in addition to modelling, consistent with that provided by ACIL Allen, which suggested that average bills under both the

¹ Energy Security Board, *National Energy Guarantee Final Detailed Design* (1 August 2018), available at: http://www.coagenenergycouncil.gov.au/sites/prod.energycouncil/files/publications/documents/Final%20Detailed%20Design%20-%20National%20Energy%20Guarantee_1.pdf

² Energy Security Board, *The National Energy Guarantee Consultation Regulation Impact Statement* (29 June 2018), available at: <http://coagenenergycouncil.gov.au/sites/prod.energycouncil/files/publications/documents/National%20Energy%20Guarantee%20-%20Consultation%20Regulation%20Impact%20Statement.pdf>



do-nothing and the Guarantee scenarios over the 2020 to 2030 period would be around \$400 a year lower than the estimated bill for 2017 due to anticipated wholesale price reductions.

However, both the Frontier and ACIL Allen modelling included benefits as a result of the full implementation of the Guarantee, assuming both the emissions guarantee and the reliability obligation components would be implemented.

Impact Analysis

The purpose of the Impact Analysis as we understand is to build on this previous modelling by presenting updated estimates of the effects of the Guarantee, reflecting updates to the policy design as well as developments in the NEM since November 2017, and then to derive estimated benefits of the RRO from that updated Guarantee modelling.

The Impact Analysis makes the same finding as the Final Detailed Design that, under the BAU scenario, projected wholesale prices will be 31 per cent lower relative to 2017-18, on average, over the period from 2018-19 to 2029-30, due to increased contributions from renewable generation (**BAU Case**).

The Impact Analysis also finds that under the Guarantee Case, average residential retail electricity bills would be around \$550 lower, on average, over the 2020-21 to 2029-30 period than in 2017-18, and that \$150 of that saving would be additional savings due to the implementation of the Guarantee (i.e. \$400 of savings are as a result of BAU reductions in the wholesale price as a result of the BAU Case). These are the same conclusions as the modelling previously provided in the Final Detailed Design.

We therefore assume that recent developments in the NEM have not impacted the modelling outcomes previously provided to stakeholders, and there are no material updated estimates of the BAU Case and Guarantee Case policy scenarios. If there are, it is not apparent to us what these updates may be from the Impact Analysis.

The Impact Analysis then attempts to assess the impact of the RRO by running a sensitivity scenario under the Guarantee Case without the additional 1000MW of renewable generation capacity expected to occur with implementation of the emissions guarantee component of the Guarantee. The Impact Analysis notes that this sensitivity scenario is considered to reflect price outcomes under the RRO.

One of the key assumptions in the modelling is that the RRO would increase contracting cover by 5%, which we note is a figure that is difficult to place with any certainty. Detailed discussion in the RIS also referenced the difficulty in precisely estimating the expected change in contract levels and apportioning this behavioural response between new and existing generators, which would have a material impact on the operation of the RRO.

While some assumptions as to the effect of the RIS need to be considered in an attempt to model any benefits associated with the policy, that uncertainty should be factored into any broad statements about the likely impact of the policy in terms of overall benefits to customers.

In running the subsequent analysis with these assumptions, ACIL Allen makes the conclusion that “retail prices are estimated to be \$110 lower on average over the period 2020-21 to 2029-30 than in 2017-18” (**RRO Case**). There is some uncertainty as to what this figure represents.

As it is stated, it appears as though the benefits of the RRO Case erode the operation of the BAU Case, which predicts that bills will be \$400 lower on average as a result of BAU reductions in the wholesale price between 2017-18 and 2029-30. If the RRO Case provides savings of \$110 in addition to the BAU Case (i.e. total benefits of \$510), this should be more clearly stated.

Requiring contracts to be physically-backed

We note the reference in the Impact Analysis to the RIS, which considered that requiring physically-backed contracts in the wholesale market could “likely decrease liquidity and competition driving up wholesale prices as a result”. That document also found that such an obligation would also likely reduce a retailer's ability to manage price risk, which could lead to higher prices for consumers.

Further work would need to be done to validate any benefits associated with requiring physically-backed contracts in the wholesale market, which would need to be carefully assessed against the possibility of consequences for contract liquidity and price as highlighted in the RIS.

Conclusion

AGL remains committed to supporting policy that provides clear long-term investment signals for the electricity sector in terms of expected commitments to reduce emissions. We note that there is still significant work to progress the RRO in terms of material settings under which it will operate such as identifying the reliability gap, methodology to assess the firmness of qualifying contracts, and the assessment of compliance and penalties, and that these settings may have impacts on the operation of the RRO and the subsequent costs and benefits that flow through to consumers.

We would expect that further assessment of the costs and benefits of the RRO continues as work to progress the detail of how it will operate continues through consultation.

Should you have any questions in relation to this submission, please contact Aleks Smits, Manager Policy & Research on 03 8633 7146, or myself on 03 8633 7252.

Yours sincerely,

A handwritten signature in blue ink, appearing to be 'Eleanor McCracken-Hewson', written over a horizontal line.

Eleanor McCracken-Hewson

Senior Manager Policy, Research & Stakeholder Engagement, AGL Energy