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Dear Commissioners



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Review of the operation of the Retailer Reliability Obligation – Consultation Paper – 23 March 2023

EnergyAustralia is one of Australia's largest energy companies with around 2.4 million electricity and gas accounts across eastern Australia. We also own, operate and contract a diversified energy generation portfolio across Australia, including coal, gas, battery storage, demand response, wind and solar assets, with control of over 5,000MW of generation capacity.

We appreciate the opportunity to participate in the Commission's review of the Retailer Reliability Obligation (RRO) as required by the National Electricity Rules (NER). We consider the Commission should broaden its review and ultimately make recommendations to energy ministers on the ongoing role of the RRO, rather than limit itself to 'operational' aspects. Investment mechanisms are now in place or in development that make the RRO redundant. The changed regulatory landscape relative to that which prevailed when the RRO was introduced significantly affects its intended operation. Exploring refinements to a mechanism that is arguably no longer needed or effective does not seem to be a prudent use of Commission or stakeholder resources. The Commission will need to eventually engage on resource adequacy settings in the National Electricity Market in reviewing the Panel's rule change proposal to amend price cap settings from 1 July 2025, and during consultation on the Commonwealth Government's Capacity Investment Scheme (CIS).

This notwithstanding, and in the spirit of constructive engagement, our submission below also identifies a series of operational issues with the RRO in line with the Commission's current terms of reference.

The Commission is able to evaluate the need for the RRO

The NER do not prevent the Commission from making broader recommendations about the effectiveness of, or need for, the RRO. The Commission is required to review the RRO under clause 11.116.18:

- (a) By 1 July 2023, the AEMC must conduct a review of the operation of Chapter 4A including any other matter which the AEMC reasonably believes is relevant to the operation of Chapter 4A.
- (b) In conducting its review under paragraph (a), the AEMC must:
 - (1) publish the terms of reference of its review; and
 - (2) follow the Rules consultation procedures.

Note

This clause does not preclude the AEMC from conducting a review in accordance with section 45 of the NEL.

The “operation of Chapter 4A” as well as “any other matter” relevant to this appears to encompass a wide scope of issues. Our view is that any evaluation of the “operation” of the RRO cannot be done without assessing how each of its components, and then the mechanism as a whole, interact to achieve the intent of the RRO as a policy intervention. This is reflected in the Commission’s proposed assessment criteria which includes encouraging efficient investment in dispatchable capacity and demand response. To the extent reviewing the “operation” of Chapter 4A places any restrictions on the Commission, the note to clause 11.116.18 explicitly preserves the Commission’s ability to undertake a section 45 review under the National Electricity Law, which can cover the “effectiveness” as well as “operation” of the rules.

In limiting itself to operational aspects, the Commission’s consultation paper refers to the Energy Security Board’s (ESB) 2018 Regulation Impact Statement:¹

This review is intended to ensure specific elements of the scheme operate as intended. The review is not intended to assess the overall efficiency of the Obligation, as determining the overall impact of the scheme would likely require a longer assessment horizon.

Somewhat contrary to the ESB’s statement, the Commission’s intention appears to be to cover an extended assessment horizon. That is, while clause 11.116.18 requires a review to be completed by July 2023, the Commission has allowed itself until early 2024. It states that this will enable it to consider the longer-term experience of the market over the seven trigger events that are either current or have been revoked.² A 2024 completion will also allow the Commission to consider the form and function of the Commonwealth Government’s CIS. The reference to the CIS is pivotal as the RRO’s effectiveness in delivering investment signals and net benefits for customers has significantly diminished in a vastly changing regulatory landscape.

The RRO will soon be redundant (if it is not already)

The RRO was introduced in 2019 as a mechanism to encourage new investment in dispatchable sources of energy generation, such that the electricity system operates reliably.

¹ ESB, *Retailer Reliability Obligation Decision Regulation Impact Statement*, December 2018 p. 51.

² AEMC, *Review of the operation of the Retailer Reliability Obligation - Consultation paper*, 23 March 2023, p. 3.

Policy and regulatory settings for investment in the NEM have been significantly impacted by the following recent interventions, some of which are still being finalised:

- The NSW Electricity Infrastructure Roadmap, including legislated targets for dispatchable long-duration storage and triggers for supplementary 'firming' technology
- QLD Energy and Jobs Plan, which also provides for explicit investment in long duration storage and triggers for the exit of existing thermal generation to ensure reliability is maintained
- Victorian Government storage targets – again underlining the focus on dispatchable technologies
- The CIS, which is explicitly designed to bring in 'firm' technologies to complement renewable investment.

All of these mechanisms were introduced after the RRO, highlighting that governments have sought clearer and more effective signals for new investment.

The presence of alternative mechanisms to ensure investment and reliability would materially alter the ESB's net benefit calculation, specifically that the RRO would deliver \$19 billion of net benefits and household bill savings of \$110 per year, relative to a "no policy" business as usual case.³ The counterfactual case now has various substitute policy interventions, meaning that the RRO's incremental effect would be marginal.

We support the Commission dwelling on the significance of the CIS in particular as it reflects the outworkings of the ESB's post-2025 work on capacity mechanisms. The ESB's last round of deliberations on resource adequacy involved a 'strawperson' proposal that sought to make the RRO effective by linking it to 'physical' supply obligations. (Of interest, such a physical linkage was not found to deliver net benefits when considered in 2018.⁴) Based on stakeholder feedback, the ESB moved further to recommend against all decentralised reliability obligations like the RRO as they were unlikely to give policy-makers sufficient confidence that new investment would take place. It seems anomalous that the Commission now appears reluctant to engage on these issues. Our expectation is that as part of upcoming deliberations on the CIS, stakeholders will be arguing that the RRO be replaced with the CIS, as was intended by the ESB.⁵

At the very least, policy-makers will need to understand any complications in having the RRO coexist with the CIS (as well as various jurisdictional-specific mechanisms). This is an area where we urge the Commission to undertake assessment as part of its current review, and its extended review timing explicitly accommodates this.

³ ESB, p. 5.

⁴ *ibid.*, p. 42.

⁵ ESB, *Capacity mechanism High-level Design Paper*, June 2022, p. 69. "The proposed capacity mechanism design would replace the existing RRO. It will eliminate the administrative costs imposed on retailers and capacity providers (such as from submitting their contracts to demonstrate compliance or via the MLO) by that scheme."

Operational issues with the RRO

The following highlight areas where the RRO's operation could be made more efficient:

- The **bid-offer spread requirements in the Market Liquidity Obligation** under clause 4A.G.18(h). In the recent highly volatile market, we expect the spread requirement (e.g. 5% for baseload products in most jurisdictions) has resulted in affected participants being forced to accumulate significant loss-making positions. In other situations, trading exchanges might absorb such losses or provide compensation where market-making is required. A potential solution could be for entities to apply to the AER for temporary relaxation or exemption from minimum price spread requirements, for example during abnormal trading conditions, or have spreads adjust dynamically in line with trailing average price observations.
- As we have raised with the AER, EnergyAustralia operates as several licenced retail entities and we consider the NER are overly restrictive in requiring the reporting of net contract positions and compliance by each liable entity. That is, **participants should be able to be assessed at a group level** and for positions to be aggregated. A disaggregated entity-level assessment requires the establishment of costly inter-entity arrangements and separate risk buffers, all subject to firmness adjustments, even though there is diversity across a broader entity-wide portfolio.
- The SA Minister has used its **discretion to make multiple T-3 instruments without breaches** of the Reliability Standard or Interim Reliability Measure and have been subsequently revoked. The Commission should comment on whether this aligns with the operational intent of the RRO, noting all jurisdictional ministers will have this power. Participants may not consider such ministerial triggers to be credible, with less incentive for proponents to inform AEMO of developments and commissioning dates that would improve any subsequent T-1 reliability assessments.
- There is potential to revisit the administration of T-3 and T-1 instruments in light of the increasing **frequency of ESOO updates**. As noted by the Commission (and recently by the AER⁶) the NER do not provide for revocation of certain instruments where respective reliability gaps subsequently close. There may be benefits here in providing participants certainty of obligations in the face of increasing uncertainty around plant entry and exit. However some **additional rigour in, or stakeholder input into, the assessment of reliability gaps** may be beneficial, particularly where reliability instruments are made on the back of developer information that is taken at face value, and are conducted under time constraints.
- We expect the Commission to liaise closely with the **AER on its administration of the RRO** and note it has received many enquiries recently given multiple instruments are now in effect. While we appreciate the AER's engagement with stakeholders, the number and varied nature of its frequently asked questions⁷

⁶ <https://www.aer.gov.au/communication/south-australia-t-1-reliability-instrument-to-remain-in-place-following-aemo%E2%80%99s-esoo-update>

⁷ <https://www.aer.gov.au/retail-markets/retailer-reliability-obligation/frequently-asked-questions>

indicates its set of guidelines could be refined. The AER is still yet to issue 'final' versions of its guidelines, after having 'interim' guidelines in place since 2019.

If you would like to discuss this submission, please contact me on 03 9060 0612 or Lawrence.irlam@energyaustralia.com.au.

Regards

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