ACOSS Submission to Energy Security Board (ESB) National Energy Guarantee Draft Detailed Design Consultation Paper

July 2018

Supported by

Who we are

ACOSS is a national voice for the needs of people experiencing poverty, disadvantage and inequality and the peak body for the community services and welfare sector.

Our vision is for a fair, inclusive and sustainable Australia where all individuals and communities can participate in and benefit from social and economic life.

What we do

ACOSS leads and supports initiatives within the community services and welfare sector and acts as an independent non-party political voice.

By drawing on the direct experiences of people affected by poverty and inequality and the expertise of its diverse member base, ACOSS develops and promotes socially and economically responsible public policy and action by government, community and business.

ACOSS would like to thank members of the ACOSS Climate and Energy Policy Network for input and guidance into this submission. ACOSS takes responsibility for final views and recommendations.

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1. Summary

ACOSS welcomes the opportunity to make a submission to the Energy Security Boards June 2018 consultation paper on the draft detailed design of the Energy Security Board National Energy Guarantee Draft Detailed Design consultation paper. ACOSS is participating in this inquiry representing the interests of people on low incomes and those experiencing the impacts of poverty and disadvantage in Australia, as well as our role as the national peak body for the community services sector.

The primary purpose of the NEG is to reduce emissions in the electricity sector. It also seeks to support efforts to address system reliability and electricity affordability.

ACOSS supports the aims of the NEG. Climate change is a social justice and equity issue that urgently needs to be addressed. People on low incomes and experiencing disadvantage will suffer most from climate change impacts as they are least able to cope, adapt and recover. A mechanism is therefore needed to reduce Australia's emissions and transition to a clean economy in line with the goals of the Paris Agreement to limit global warming to well below 2 degrees and pursue a limit of 1.5 degrees. The transition should be achieved in a least cost, equitable and inclusive manner, to ensure that low-income and disadvantaged households are not left behind nor pay disproportionately more for the transition.

The majority of ACOSS's concerns with the NEG largely relate to the Australian Government's design elements. These concerns go to ambition, equity and affordability that are detrimental to low-income and disadvantaged households. The latest ACOSS figures identify 3 million people, including over 731,000 children, already living in poverty in Australia, the number of people struggling with energy stress is likely to be much higher.

ACOSS has made a separate submission on the Government design elements[1] calling for:

- The 2030 emissions reduction target for the electricity sector to be increased in line with the electricity sector's ability to decarbonise faster than other sectors and with what Australia should be doing to contribute to achieving the Paris Agreement [climate change] goals;
- Inclusion of triggers to increase the target outside of review periods;
- Enable state targets to be additional on an opt in basis;
- Energy Intensive Trade Exposed industry (EITEs) not to be excluded from the emissions reductions mechanism, as this will shift costs to other consumers; and
- Offsets not to be included.

On the design elements of the NEG mechanism, ACOSS acknowledges the continued improvements to the design to support competition, reduce complexity and improve affordability of the scheme. ACOSS also acknowledges that the NEG could provide a durable framework for energy and climate policy under ambitious emissions reductions, but we struggle to see the benefit under low emissions targets where costs are likely to outweigh the benefits. The exclusion of EITEs remains a significant barrier for ACOSS, because of the cost shifting and lack of evidence for the exclusion.

The ESB has sought feedback on proposed new design elements. Utilising a table format ACOSS has indicated our position on new proposals (where they are of material relevance to low-income and

[1] https://www.acoss.org.au/wp-content/uploads/2018/03/ACOSS-Final-Submission-to-ESB-on-NEG-Discussion-Paper.pdf

disadvantaged households) and provided additional recommendations that focus on improving equity, scalability, competition, compliance and reduce cost.

To help evaluate the effectiveness of any emissions reductions mechanism's ability to protect people on low incomes or experiencing disadvantage, ACOSS in consultation with a range of members has developed a set of principles outlined in Appendix 1. We have used these principles to judge the effectiveness of the NEG and in responding to the consultation paper questions.

2. ACOSS comments and recommendations on draft detailed design

Element (reference)	Draft Detailed Design	ACOSS Comment/recommendation
Emissions Reduction Mechanism		
Competition measures in emissions obligation (ESB 3.3.2)	In place of its controlling corporation responsibility element, ESB proposes several measures in the Emissions Obligation to foster competition: • The first 50GWh of a market customer's load would be exempt from the emissions obligation. The intent is to support retail market competition by making life simpler for small retailers. The exempted load would be spread across all other market customers, to ensure that overall targets are met. • New obligations on generators and market customers not to unreasonably withhold allocations from market customers. • Administrative requirement on generators to allocate all generation by the reporting and compliance date.	• ACOSS supports the new additional measures to support greater competition in generation and retail.
Accounting for generation and Load - EITE exemption (ESB 3.3.3)	Exempt EITE load would be added back onto non-exempt load, by scaling it up after the compliance period. AEMO would publish a weekly estimate of how this scaling factor is tracking, based on EITE and non EITE load.	• ACOSS emphatically opposes the exclusion of EITEs and urge NEM States and Territories to also oppose the exclusion. The NEG is modelled to put downward pressure on wholesale prices, so it remains unclear why EITEs should be exempt. EITE demand is around 20% of the total NEM demand. To the extent that there are emissions compliance costs, an un-exempted user will pay around 20% more for these than without an EITE exemption. These costs will be smeared across bills, where low-income and disadvantaged households pay disproportionately more of their income on electricity and will be worse off as a

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		result of the exemption of EITEs. ACOSS calls on ESB to be transparent about the costs that will be shifted to other consumers as a result of the policy of excluding EITEs. • If the policy to exclude EITEs is implemented there should be at a minimum (a) a clear pathway for the exemptions to decline and (b) annual publication of the costs to other consumers of the exemption.
Accounting for generation and Load – Greenpower and Voluntary action (ESB 3.3.3)	The ESB proposes to facilitate the treatment of GreenPower in the emissions reduction requirement to allow consumers to make an additional contribution to emissions reduction beyond that required by the target. The discussion paper notes that including Greenpower in the NEG may not be as straightforward as its inclusion in the RET. The ESB intends to work with the National GreenPower Steering Group to find a way to achieve the policy goal of additionality within the framework of the Guarantee.	• ACOSS supports the inclusion of Greenpower and hopes the ESB and National GreenPower Steering Group find a way to achieve the policy goal of additionality within the framework of the Guarantee. • ACOSS also recommends that the ESB explore a mechanisms for market participants who overachieve, as well as State, business and others who undertake action to reduce emissions associated with their electricity use (outside of Greenpower), to also make voluntary additional contribution to emissions reduction beyond that required by the target. Under the current functionality of the Renewable Energy Target registry consumers are free to purchase renewable energy independent of their electricity retailer which they can then retire from being used by anyone else to meet legal obligations. This is via the voluntary surrender function within the registry. There is a need to allow parties other than retailers to be granted the abatement rights to their low emission generation

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		by the regulator so they can be free to do with it what they wish. This includes voluntarily extinguishing it so that retailers have to make extra efforts to reduce emissions.
Registry Operations (3.3.4)	The registry provides the necessary infrastructure to facilitate efficient compliance with the emissions reduction requirement. It allows market customers to be allocated a share of a generator's output and associated emissions, and to present this for the purposes of compliance in respect of their load. It is proposed that the registry will be administered by AEMO, as an enhancement to its existing systems. The AER will have complete access to the registry to facilitate its role in monitoring and enforcing compliance. The registry will only be accessible to market customers and generators. Some information will be made public at given intervals, such as overall scheme performance and market customers' overall emissions intensity.	• ACOSS supports increased public transparency of the NEG registry. Concerns have been raised that the proposed NEG registry lacks transparency. Unlike the Renewable Energy Target (RET), which operates a similar registry system where anyone can gain complete free access and transparency, only market customers and generators can access the proposed NEG registry. The free flow of market information can act to maximise market efficiency and avoid situations of sudden abrupt movements in price and market manipulation, and can act to support potential new entrants and competition. We urge the ESB to consider ways to increase transparency while protection commercial in-confidence information and look to the RET registry for guidance.
Flexibility compliance options (3.4)	3.4.1 Carry forward over achievement - Market customers will be permitted to carry forward a limited (5% of emissions intensity load or fixed amount of 60,000 tCO2-e) amount of a previous compliance year's over-achievement, for use in a later compliance year. This is expected to incentivise investment when the market needs it and should enable market customers to achieve compliance at a lower cost.	• In principle ACOSS supports the proposed limit on carry forward of over achieving outlined in 3.4.1, noting our understanding is that this requirement does not prevent a market customer from unlimited over achievement. • ACOSS is concerned the process to defer compliance outlined in 3.4.2 is too generous, especially when combined with the weak penalty regime. At a minimum it should be reduced after first fee years of the mechanisms operation.

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	3.4.2. Deferring compliance - market customers will be able to defer 10 per cent of the electricity emissions target per MWh of load. The limit will be cumulative over two years, with the market customer required to make good in the third year on the first year's deferral amount. 3.4.3. Use of Offsets - The Commonwealth Government is continuing to consider whether market customers should be able to use external offsets as a flexible compliance option to meet the emissions reduction requirement.	• ACOSS does not support the use of offsets to achieve emissions reductions in the electricity sector as raised in 3.4.3. There has been no modelling to test whether inclusion of offsets would drive down costs of the transition. Offsets would reduce investment in new clean generation locking in higher emitting technology for longer and hinder achieving reliability obligation, both of which could increase costs to consumers.
Reporting and compliance (ESB 3.5)	3.5.1 The AER as enforcement agency for the NEG - the AER will draw on a range of enforcement tools that already exist under the NEL. The AER will report annually on high-level compliance outcomes for each compliance year, by 31 December following the compliance year. The information published will identify by name all market customers and their emissions intensities for the given compliance year. 3.5.2 The compliance period - The compliance period for the emissions reduction requirement will be on a financial year basis. 3.5.3 Reporting and Administration - Where possible, the reporting required to assess compliance will build on existing data sources (for which the existing frameworks for monitoring and enforcing reporting	• ACOSS supports the ESB's recommendations at: ○ 3.5.1 Giving enforcement responsibility to AER ○ 3.5.2 compliance period ○ 3.5.3 Including introducing anti-avoidance regime to prohibit restructuring for the purpose of avoiding obligations. • With respect to section 3.5.4 Enforcement tools for emissions reductions requirements, while facilitating a culture of compliance can be beneficial, it's important to the integrity of the Emissions reduction mechanism that strong signals are provided to avoid non-compliance. ACOSS believes that retailers will be well aware of their obligations and like the Reliability Obligation the Emissions Obligation compliance regime should skip straight to a penalty process based on share

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	requirements will continue to apply). Where new information is required to assess compliance, such as emissions data for generation not currently captured in NGER, additional reporting requirements will be introduced. The ESB is considering the merits of introducing an anti-avoidance regime in the NEL that relates to the Guarantee. This is intended to prohibit an entity which has a potential obligation under the Guarantee from restructuring or taking other action for the purpose of avoiding or minimising that liability. 3.5.4 Enforcement tools for emissions reduction requirement – The AER already has access to a range of compliance tool. The AER will publish guidance on the enforcement options. The ESB notes the primary approach will be to build a "culture of compliance" minimising non-compliance through information and education and annual reporting of compliance. AER could then initiate civil proceedings in court for alleged breaches and that civil penalties with a new upper limit of $100 million apply. The ESB outlines some additional enforcement options including administrative action, infringement notices, and court enforceable undertakings.	of business revenue followed by suspending or revoking authorisation to operate in the retail market.

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Reliability Obligation Mechanism		
Forecasting the reliability requirement (ESB 4.2)	ESB states that "AEMO will continue to work with the Reliability Panel on the appropriateness of the current Reliability Standard in the face of an increasingly 'peaky' supply-demand balance. The intention of the Guarantee is to remain aligned to the Reliability Standard while ensuring there are adequate resources available to meet peak (as opposed to average) demand."	• ACOSS supports the current reliability standard of 0.002%, and supports ESB intention for the Reliability Obligation Mechanism to remain aligned with the Reliability Standard. It's also important that the same reliability standard is used to determine additional investments under the Reliability and Emergency Reserve Trader (RERT) if it's triggered as part of the Procurement of Last Resort stage of the Reliability Obligation. ACOSS notes that in 97.2% of circumstances disruption are a result of distribution interruptions and not generation failures. A tighter reliability standard would likely lead to over investment and increased costs to consumers, as we saw with networks in early 2000s.
Triggering the reliability requirement (ESB 4.5)	ESB proposes a decision on triggering the Reliability Obligation by an independent entity (AER) if AEMO requests such a trigger three years out from a projected shortfall. We understand the ESB has also requested feedback on a stakeholder proposal, made at the 2 July forum, that the three year trigger be scrapped to simplify the process – leaving a regular forecasting update process and an AEMO decision on procurement-of-last-report (and associated Obligation compliance) one year out from a forecast shortfall.	• ACOSS supports the requirement for an independent entity to provide a check on a request by AEMO to trigger the reliability obligation, and supports the AER being assigned to this role. • It is essential the obligation is only triggered where it is clear the benefits to consumers outweighs the costs. ACOSS supports PIACs submission that calls for objective criteria as to whether a material reliability gap is forecast to exist and whether the gap will be persistent and not just a blimp. • ACOSS would prefer a clearly defined compliance trigger, so as to provide the market certainty as to when compliance will be required.

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	The basis for the assessment of materiality must be clearly defined and transparently communicated to support liable entities to predict their potential liability and to close the gap as efficiently as possible. Determining whether a reliability gap is 'material' requires a balance between certainty and predictability together with flexibility to accommodate changing market conditions. This can be achieved by the use of more objective criteria such as a percentage of maximum demand in a region persisting for a given period of time. The Rules will set out a transparent framework to allow AEMO (and the independent entity) to determine the materiality of a reliability gap. This could be similar to that which applies to reviews of the market reliability settings by the AEMC's Reliability Panel. The framework will specify: • The timing of the materiality assessment. • Prescriptive requirements which must be adhered to as part of the materiality assessment. • A requirement that AEMO must publish a guideline, as part of the annual ESOO development consultation process, outlining how it will determine materiality. • How a material gap, and decision to trigger the reliability obligation, is communicated to market participants.	• ACOSS does not have a fixed view on whether 3 years is the best time frame. We note ECA in their submission raises concerns with the time frame arguing the longer the period between the trigger point and the reliability gap could lead to a greater risk that un-needed investment in capacity demand response occurs which consumers bear the costs. This of course needs to be balanced with appropriate time frame to make investments. ACOSS suggests a shorter timeframe say 2 years may be adequate and reduces risk of unnecessary investment and unnecessary compliance costs. • ACOSS in principle supports the process ESB has set out to define the reliability gap to ensure it is "sufficiently material", including the "gap persisting for a given period of time". ACOSS supports PIACs submission advocating for the reliability gap to be expressed not only in terms of Unserved Energy, as this aligns with how the Reliability Standard is expressed, but also in other terms which are more immediately relevant to sizing and procuring efficient solutions. For example, the forecast should also give guidance as to whether it would be a short-lived event or a more sustained event. It should also give guidance as to whether it is likely to be a single event during the forecast period or whether it may be recurring over multiple days or weeks. In addition ACOSS supports the ECA submission advocating the AEMO should be required to identify the reliability gap specifically and clearly to allow fit-for-purpose contracts and associated responses to be established. The

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		description of the gap should also be clearly and explicitly linked to the basis upon which the reliability obligation can be triggered by AEMO.
Qualifying contracts (ESB 4.6)	If the reliability obligation is triggered, liable entities will be required to enter into sufficient qualifying contracts to cover their share of system peak demand at the time of the reliability 'gap' to meet possible future compliance. ESB outlines 5 options for accessing contract and proposes that qualifying financial contracts must either have been bought on a centrally cleared market or recorded in a trade repository of OTC derivatives; and that a Market Liquidity Obligation (MLO) apply to large gentailers, obliging them to offer contracts on a centrally cleared platform during a reliability gap and post bid and offer spreads. The ESB also seeks feedback on whether the previously flagged voluntary 'book build' coordinated by AEMO would still be needed if an MLO applied. The 'book-build' will be conducted by inviting sellers to make offers to sell new contracts for the duration of the gap and for buyers to make offers to buy new contracts. AEMO will aim to match buyers and sellers in a way that delivers the maximum closure of the gap.	• ACOSS agrees that framework to define qualifying contracts should not be prescriptive and instead should incentivise the development of new innovative contract products. • ACOSS also supports ESB recommendations to aggregate all qualifying contracts over the period of the gap rather than provide all individual contracts, which should help reduce costs of compliance. • With respect to mechanism for accessing qualifying contracts the ESBs preference to combine Market Liquidity Obligation with a trade repository and reporting requirement, seems preferable to Centrally Cleared Contracts in order to incentivise new product development. To this end ACOSS would also support inclusion of the Voluntary Book-Build Approach, which would enable smaller retailers and other entities to provide innovative products to meet reliability. • ACOSS strongly supports inclusion of a demand response mechanism in the wholesale market, which is likely to be the least cost way to meet peak demand and drive prices down.

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	Demand response contracts could also qualify (as distinct from financial contracts where the seller may use many physical means including demand response to manage their financial risk).	
Penalties (ESB 4.9)	The first stage of the penalty framework for the reliability obligation will allocate costs to liable entities which have failed to meet their contractual obligations. A liable entity found to be non-compliant will be charged a predetermined proportionate cost per MW of non-compliance to refund a proportionate cost of the Procurer of Last Resort costs to consumers. In the **second stage**, the AER will retain its ability to apply its usual suite of enforcement options in addition to the assignment of RERT costs in stage one. Including civil penalties "the ESB considers up to $1 million would be an appropriate upper limit on first offences, with up to $10 million the upper limit on repeat offences."	• ACOSS supports the inclusion of a penalty framework including allocating costs of meeting reliability to uncompliant retailers. However, it is not clear to ACOSS whether the provision to allocate costs of the Procure of Last Resort will be fully covered by a "liable entity found to be non-compliant" or if only a portion of costs will be covered and consumers will foot the bill for the rest. ACOSS does not support consumers footing the bill for "Procure of Last Resort" and urges the ESB to make it clearer how costs will be recovered. • ACOSS suggests the ESB consider defining penalty as shares of business revenue as a greater deterrent.

Appendix 1 – ACOSS key principles in designing an emissions reduction mechanism for the electricity sector

An emissions reduction mechanism:

- Must be credible, scalable and durable, in line with the goals of the Paris Agreement to limiting warming to well below 2 degrees and pursue a limit of 1.5 degrees C (The adherence to Paris Agreement trajectory is important to reduce cost on future generations)
- It should contribute to low-income and disadvantaged households being better off with lower costs and safer climate.
- It should be effective and efficient including:
  - Least cost;
  - Facilitate well-functioning, open and low cost energy market (i.e. does not lead to market distortion, barriers to entry, market concentration and over investment);
  - Efficient and transparent pass through of costs.
- It should be fair and equitable.
- Governments should collectively carry the costs of the mechanism. Where this is not the case, scheme costs should be allocated equitably and measures put in place to offset disproportionate costs to people on low incomes and experiencing disadvantage (because low-income and disadvantaged households pay disproportionately more when costs are smeared across bills).
- It should provide a degree of certainty to support a just and managed transition for workers and communities affected by the transition from fossil fuels to clean energy.
- The energy sector can and should transition faster. Emissions reductions should come from within the electricity sector, without use of offsets.
- Complementary measures should be introduced to further address other parts of the quadlemma with respect to affordability, reliability/security, and a just transition.
- Not all members of the community have the capacity or inclination to engage in the energy market, and should not be penalised for not doing so.
- Community interests, in particular those on low-income and experiencing disadvantage, should be actively engaged or represented in the design of the mechanism.