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Electricity Infrastructure Roadmap: Infrastructure Safeguard (Part 6 of the EII Act)

AGL Energy (AGL) welcomes the opportunity to comment on the Department of Planning, Industry and Environment's (DPIE) consultation paper on tranche 3 regulations for the Infrastructure Safeguard.

AGL is a leading integrated essential service provider, with a proud 184-year history of innovation and a passionate belief in progress – human and technological. We deliver 4.2 million gas, electricity, and telecommunications services to our residential, small and large business, and wholesale customers across Australia. We operate Australia's largest electricity generation portfolio, with an operated generation capacity of 11,208 MW, which accounts for approximately 20% of the total generation capacity within Australia's National Electricity Market.

AGL provides the following comments on each of the topics raised by DPIE in the consultation paper.

Guiding Principles

The consultation paper outlines a number of principles that will be used by DPIE in making policy decisions related to the Infrastructure Safeguard. These include:

1. ensuring frameworks are fit-for purpose and reflect industry best practice
2. providing flexible arrangements to allow for innovation and changing market conditions
3. transparency of functions and processes relating to the Safeguard
4. alignment with NEM processes to support efficient markets
5. ensuring community support (social licence) through well coordinated infrastructure development
6. adequate oversight of the consumer trustee and managing key risks.

AGL suggests DPIE should also explicitly consider ways to minimise the costs of the scheme for the benefit of NSW consumers. This is an important consideration for all aspects of developing the NSW Roadmap, including the topics to be considered in the Infrastructure Safeguard regulations. Cost minimisation would be balanced against other objectives, checks and balances that are equally important but may otherwise increase the administrative costs of the scheme.

Planning for private sector infrastructure investment

The consultation paper sets out the process and inputs for preparing the Infrastructure Investment Objectives (IIO) report every two years, which includes the 20 Year Development Pathway and the 10 Year Tender Plan. The Consumer Trustee will need to make assumptions regarding the closure of power stations, the development of inter-regional network infrastructure, changes in technology



costs and other market developments as in developing the IIO report, and the consultation paper seeks views on how this should be assessed.

It's not entirely clear from the EII Act or consultation paper whether the IIO report will be an engineering-based report (like the ISP) or will involve economic modelling that takes into account the commerciality of projects. We envisage that at least in the first years of the IIO report it will be a subset of the ISP that is focussed on NSW and how to deliver the capacity build targets for 2030. As a subset of the ISP, the IIO report should not seek to duplicate or change the ISP.

Beyond the 2030 targets, the IIO report would ideally assess the ideal timing of new entrant projects given expected market prices. The appropriate form of consultation and inputs will somewhat depend on what the IIO report is seeking to achieve.

Question 1: What requirements for stakeholder consultation on the IIO Report should be implemented to ensure the Consumer Trustee's report is informed by the best available information?

Stakeholder consultation will be an important check and balance for the Consumer Trustee to make sure the most up to date information is used as an input to the IIO Report.

However, to the extent that the Consumer Trustee is using the same scenarios or assumptions as the ISP, it would not be necessary to carry out the same level of thorough consultation as the ISP process. This would avoid unnecessary duplication of efforts for both the Consumer Trustee and industry participants.

For example, it would be unnecessary to reassess the ISP scenarios and weightings, which are developed through a very involved consultation process and through the Inputs Assumptions and Scenarios Report process.

Question 2: How should changes in technology, consumer behaviours, customer investment in generation (e.g. distributed energy resources) and demand uncertainty be treated to determine the requirements for large-scale infrastructure investment?

These trends will need to be considered in the IIO report as these will have a direct impact on the requirements for large scale infrastructure investment. Stakeholder engagement directly with experts on these topics will be important to track developments in these areas over time.

While the IIO report spans the 20 year development pathway, there will be uncertainties that mean the IIO report can only be based on the best information of the time it was produced. The Consumer Trustee can consult to ensure its assumptions are as robust as possible, and the IIO report will be updated every two years with better information. As the outcomes over the short or medium term are more certain than longer term outcomes, the 20 year development pathway needs to be robust to different scenarios, which will then become more certain with subsequent IIO reports.

Question 3: What assumptions, scenarios or approaches could be prescribed by regulation to encourage an independent Consumer Trustee to make appropriate decisions regarding the treatment of future risks and uncertainties in planning for infrastructure investment?

There are two aspects that we suggest the IIO report consider carefully:



- The optimal split between wind and solar generators to be supported in a REZ, given the capacity of the REZ and their different generation profiles.
- How to forecast whether thermal generators will close earlier than expected. One option is to use the reported closure years. A second option is to undertake economic modelling that incorporates the impact of new generation on wholesale prices and to make assumptions about when thermal generation may exit the market based on those prices. Alternatively, modelling could involve sensitivities that include earlier exits.

However, we do not necessarily suggest that these issues need to be prescribed in regulations.

Policy questions for LTESA

Question 4: What role could demand response play as ‘firming infrastructure’ under the EII Act and are any special considerations required in LTESA design?

We note that the types of demand response that could participate as ‘firming infrastructure’ under the Roadmap is currently limited, given the requirement that the demand response would need to participate in central dispatch to be eligible (that is, through the Demand Response Mechanism (DRM) or as a Scheduled Load). The DRM has only recently commenced.

As a general principle, AGL is supportive of demand response being treated on equal terms with other firming generating assets and being provided similar opportunities to access support through LTESA. Demand response that is participating in central dispatch is competing with other generators to access the spot price and therefore it appears equitable that it should also be able to compete for LTESA that protect against periods of low prices. The investment costs for the customer to install behind the meter equipment can be significant. Having certainty of payments over a payback period are often necessary to justify the investment.

However, there are many differences between demand response and traditional generation that would need to be considered in designing an appropriate LTESA, which should be the subject of a more specialised and targeted consultation in the future. Some initial considerations are set out below.

1. Demand response can involve a customer reducing its load or activating behind the meter generation. Each of these have different characteristics with regard to how often and for how long they can be activated. This indicates that LTESA design may be quite different to other firming generation projects, and may need to be bespoke for different types of demand response projects.
2. Renewable generation projects are required to be at least 30 MW in size to access LTESA. Demand response is typically much smaller, even at aggregated levels. The minimum size requirement for participation in the DRM is 1MW. DPIE may want to consider an appropriate size requirement for demand response to access LTESA.
3. The contract length may need to be negotiable, depending on the customer’s needs, investment requirements and appetite for commitment. While some customers may be in a position to commit to five or more years, others may only be in a position to contract for 1-3 years at a time.



4. The lead time to invest in a demand response project is much shorter than traditional generation and is typically less than a year. In participating in a LTESA tender process, it may be problematic for customers if the commencement date is years in the future.
5. DPIE may wish to consider interactions with the incentives for demand response under Peak Demand Reduction Scheme, for example to ensure there is no inappropriate 'double-dipping'.
6. DPIE may find it challenging to compare demand response projects against other types of firming generation for LTESA, given the potentially significant differences in lead times, activation preferences and financial contract structure. As noted above, AGL strongly suggests further consultation on the design of firming LTESA and how such an agreement might be financially structured, to better understand these issues.

Question 5: Other than those prescribed in the EII Act, are further LTESA design principles required to support spot, contract and system service market operation and greater consistency across jurisdictional schemes and, more broadly, innovation over time?

The Consumer Trustee is required by the EII Act to consider the following principles when determining terms and conditions for LTESA:

1. Aligning the financial terms of the LTESA with the changing needs of the energy market
2. Using conventions and standards similar to other agreements in the NEM
3. Accounting for possible future changes in NEM design (eg security services or capacity mechanisms)
4. Ensuring consistency with the Risk Management Framework (discussed further below)

The Consumer Trustee will be making decisions about the structure and terms of LTESA which will be binding on and will need to be managed by the Scheme Financial Vehicle (SFV), for by entering into contracts. It will be important that the Consumer Trustee considers the ability of the SFV to manage these risks, in making decisions about LTESA structure and terms, to minimise the costs of the scheme for NSW consumers.

It may also be appropriate that the Consumer Trustee is provided some flexibility to develop different LTESA structure and terms over time, to accommodate new technologies or other innovative projects. There should be an appropriate consultation process at the time, should this occur.

Tendering for and recommending LTESA and access rights

Under the EII Act, the Consumer Trustee is able to recommend a renewable project for a LTESA that is not inside the REZ if it shows 'outstanding merit'.

In the consultation paper, a starting point for determining whether a non-REZ project shows outstanding merit is to ensure it delivers better outcomes for consumers and communities when compared to similar projects built inside a REZ.

Question 6: What do you think is important to include in a regulation to define 'outstanding merit'?

There are numerous circumstances in which it's in the best interest of NSW consumers and communities to allow and encourage generation projects located outside a REZ, and these projects should be able to access LTESA. AGL suggests that any definition or guidance for



'outstanding merit' set out in the Regulations should be flexible enough to allow for a wide range of circumstances and benefits that may not be identified through this round of consultation.

Below is a list of examples where there would be benefits in offering a LTESA to a renewable project outside of a REZ, however we consider the Consumer Trustee should retain discretion to consider benefits beyond this list:

- The project is lower cost than projects located within the REZ
- The project is located in a part of the network that would not cause network congestion (eg there is pre-existing capacity)
- The energy output of the project is correlated with periods of peak demand
- The energy output of the project is non-correlated with output from REZ generators
- The project is able to provide other valuable system services
- The project has strong community support

More generally, there are locations across NSW that would be excellent for renewable projects which may not be in a declared REZ. For example, a project may wish to utilise an existing generation or load site, or locate near an excellent renewable resource (e.g. offshore wind or biomass), or for an innovative reason not yet contemplated. In developing this Roadmap (and other energy market reforms), project developers should be encouraged to find the best possible locations and innovative options for projects, as this will deliver the best outcomes for NSW consumers. NSW customers should not miss out on cost savings or a more secure or reliable system simply because a project is not located in a REZ.

AGL is also concerned that development of the Energy Security Board's "Congestion Management Model - REZ" will mean that new developments are penalised for not locating within REZ and will effectively be subject to approval from the transmission planner. The CMM REZ will be considered further and designed over the next 12 months, and AGL suggests that DPIE closely consider the impacts of this policy on Roadmap outcomes throughout the development process.

Question 7: Are there further matters that should be considered when setting and using REZ access fees?

In setting the REZ access fees, the Consumer Trustee is able to set different access fees for different types of infrastructure or for projects with different access rights. For example, projects that help to increase the network hosting capacity and utilisation could be offered a lower access fee to encourage those projects to locate within the REZ.

There may be circumstances where a REZ is declared and built around an existing generator. AGL suggests that the existing status of these generators should be recognised in some way – either through exempt or heavily reduced access fees. These generators would not have access to support through LTESA and would be disadvantaged compared with comparable new developments in the REZ.

AGL is strongly of the view that NSW consumers should only pay for benefits that they receive, and not for indirect benefits which accrue to others. Non-market benefits such as emissions reduction, regional employment, or regional investment are all key aspects of the energy market transition, however the costs of these benefits should only be borne by the communities that benefit, or paid by taxpayers more broadly (through governments). AGL suggests that DPIE closely



consider the cost elements that will be recovered through REZ access fees versus cost recovery through distributors. Certain local benefits such as the community and employment purposes would be more appropriately recovered through REZ access fees, however this should not result in a greater proportion of other costs being recovered through distributors in order to keep REZ access fees low. The Consumer Trustee should carry out further consultation on REZ access fee structures as they are being developed.

Governance and controls

As noted in the consultation paper, the Consumer Trustee will need to manage a number of risks and decide on its risk appetite and how to make trade-offs, in light of uncertain future outcomes. Ongoing transparency and accountability in decision-making by the Consumer Trustee is critical to ensuring the Infrastructure Safeguard is effective and maintains the confidence of all stakeholders. The Risk Management Framework will outline how the interests of NSW consumers will be protected.

Question 8: How should stakeholders be engaged in key processes so as to ensure the ongoing success of the Infrastructure Safeguard according to the objectives of the EII Act?

Confidence in the Consumer Trustee and Roadmap will be assisted through a robust governance framework that includes stakeholder consultation, transparency of decision-making, reporting of outcomes and monitoring by the Regulator.

Question 9: Where could the regulations provide guidance to the Consumer Trustee in relation to the risk management framework, to increase transparency and confidence for stakeholders?

No response.

Question 10: When should the Scheme Financial Vehicle enter hedging contracts?

AGL has previously raised concerns that the SFV may find it difficult to package and on-sell the generation LTESA at a good price. Even contracts with a fixed shape and volume are unlikely to be valuable to the market, given the high correlation with other renewable output from those regions and typically lower prices seen during those times. The SFV will be competing with any other participant selling shaped contracts. Additionally it's unclear who would be interested in buying these shaped contracts from the SFV during years where LTESA options are exercised, which are more likely to be years of depressed wholesale prices.

It's also unclear whether the SFV intends to sell derivative contracts to manage risk, or to sell contracts that are linked with particular assets. The SFV is unlikely to be able to on-sell a contract as a "green" contract to interested buyers unless it is a generation following PPA. A fixed shape contract from a wind or solar project can not be sold as a "green" contract because it's not linked to the actual physical generation of that plant.

Regardless of these concerns, AGL broadly agrees with the principle that the SFV would enter contracts to manage its risks of liabilities under LTESA where doing so would reduce the costs of the scheme to NSW consumers.

However, the SFV should not be required to hedge the risk of LTESA. The SFV will be a significant player in the NSW contract market and should not be put in a position where it is forced to sell



below the prevailing market price, as this would have negative impacts on both NSW consumers and other NEM participants. We suggest that development of the Risk Management Framework and the approach of the SFV is transparent.

Question 11: What capabilities will the Consumer Trustee or Financial Trustee need to manage net exposures under hedging contracts and LTESAs?

The Consumer Trustee / Financial Trustee will need a deep understanding of Australian energy markets and extensive experience in derivative trading, through both the ASX and OTC markets (with ISDA counterparties and brokers) to effectively manage net exposures under hedging contracts and LTESA, and understand how to create contracts and shapes that counterparties are interested in buying. It will need an Australian Financial Services Licence to undertake these activities.

Question 12: What parameters, principles and structures should be regulated to limit net basis risk exposures for consumers?

The consultation paper does not specify whether a cap on net basis risk would apply to entering into the generation LTESA, or on the subsequent hedging by the SFV.

If you have any queries about this submission, please contact Jenessa Rabone or [REDACTED]
or [REDACTED]

Yours sincerely,

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