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Dr Kerry Schott
Chair, Energy Security Board
info@esb.org.au

Dear Dr Schott,

Re: National Emissions Guarantee Draft Detailed Design for Consultation

Flow Power is pleased to have the opportunity to have input on the National Emissions Guarantee Draft Detailed Design for Consultation. For a growing business, we have committed substantial time, energy and resources to this issue given its significance and importance. Our business outcomes, which are projected to have continued and rapid growth moving forward, are clearly demonstrating the increasing value being obtained through (C&I) customers being “connected to the market signals”.

Further details about who Flow Power is and how it operates in the market can be found in our submission to the draft consultation in March 2018. Flow Power is already dealing with and managing a number of the challenges identified in the consultation paper. Flow Power’s Corporate PPA model is playing an important role in supporting the development of large scale renewables by providing price confidence to investors. As our model values developments that are positively correlated to the spot market price and our customers’ demand profiles, we will continue to first and foremost support best fit, cost effective solutions.

It is our firm belief that this will increasingly provide substantial value to business customers (by prioritising operations based on their business requirements and pricing profile) and to the market as a whole. Any change in arrangements must act to support and further enhance price signals that are fundamental to how this value is obtained.

Flow Power maintains the following concerns with respect to the current design mechanisms:

- Most of the work completed to date, including much of the Technical Working Papers, continues to include high level design details that account for the current power system rather than evolving developments;
- As we saw with network gold-plating, it appears many of the NEG obligations will result in worst-case scenario planning locking in potential forecast errors, thereby potentially removing the pricing signals that may otherwise drive the investment (or divestment) required.

We raised several items in our initial submission in March that we feel are yet to be fully explored, namely:

- Arrangements associated with the guarantee must ensure transparency and liquidity in contracts associated with satisfying the reliability and emissions obligations – simply entering these items into a registry for compliance does not necessarily ensure suitable price discovery (as witnessed in the LGC market);
- The treatment of demand response is still particularly concerning and may discourage adoption due to NEG compliance concerns

We have elaborated on some of these concerns with practical examples where possible in the following detailed response section.

Although we thank the ESB for its interactions with our business in recent months, we still affirm there is much more detail that needs to be addressed and worked through before final ratification occurs, even if this means slowing down the current consultation rate in the interests of getting it right now. A far worse outcome would be to race the implementation 'in the National Interest' only to be back at the drawing board within a few short years!

If you have further questions please contact Liz Fletcher on 0417 080 535 or email liz.fletcher@flowpower.com.au

Kind regards



Matthew van der Linden

Managing Director

Flow Power

Detailed Response

The follow responses are in relation to specific concerns noted above and throughout the draft detailed design consultation paper. Our responses follow the same basic notation as the paper for simplicity with the corresponding reference to the consultation paper.

Safeguarding Competition (2.7)

Whilst we note the ESB's acknowledgement of smaller retailer concerns in this area, the responses do little to ensure the 'enhancement of market liquidity and pricing transparency'.

- There continues to be an underlying thread in the papers that spot-exposed consumers and even demand-response sensitive customers need to be discouraged. Similarly, how a retailer (particularly a small retailer) would deal with this type of entity is yet to be fully explored and we would request far greater development of this type of scenario, rather than simply designing a system for the 'usual business practise'
- The over/under achievement requirements require further work to ensure that the reason for the under/over achievement are outside of the retailers control. An example would be a customer with a significant load that is temperature (or irradiance) dependent – the eventual load on the day would only be known once the day had commenced.
- The Market Liquidity Obligation needs far more work and development, particularly if it is forcing particular bid and offer spreads for swaps in a region. A contemporary example would be the 500MW obligation imposed by the ACCC on AGL in NSW in 2013 during the Macquarie Generation examples. Flow Power has very little understanding as to whether trading may or may not have occurred, at what bid/offer spread was observed. Replicating this mechanism would be pointless.
- The concept of a voluntary book-build by AEMO (as stipulated in the 'TWP – Book Build' paper) would be concerning, as it implies such a process is simply the aggregation of demand and supply elements that can be simply 're-run' and 'voluntary' as required. Although AEMO would have access to some of the information required for such a process, the nature of AEMO and its skills/resources would be questionable from our opinion – this is far better sitting with other entities such as third-parties, where costs, risks and prices can be fully explored. This keeps AEMO free to determine the gap rather than having to solve the problem as well.

Emission Reduction Requirement (3)

Flow Power has the following statements:

- Ensure that the target can be reviewed upwards within a reasonable timeframe to adapt with the changing power market; and
- Do not allow the use of external offsets for meeting obligations under the NEG

Flow Power sees price as the ultimate equaliser, and so affirm that it is important future generation sources are introduced strategically and that it is a market led (and priced) plan rather than a plan with significant regulatory dislocations or price impediments.

We agree with the AER having a strong role in the compliance mechanisms as noted in the consultation paper, if the AER is:

- Adequately resourced and skilled to internally execute such requirements (ie limited use of external contractors and third-parties); and
- Given the sensitive nature of the material they will be administering (all contractual and emissions information), suitably secure and confidential.

The 'residual' emission intensity value needs further consideration and should not just be 'the leftovers' that will be applied to anyone who has not decided to contract its generation volume for various price, risk or timing reasons. In order for this to be a considered and priced decision, further information will be required.

Reliability Requirement (4)

Flow Power welcomes the enhancements noted in the consultation paper, but maintains a number of concerns:

- Forecasting the reliability requirement (as currently planned) will be extremely difficult and if devoid of price and probability, not helpful for retailers in determining what actions it should take to minimise risks. A 50MW gap in South Australia will be priced significantly different than a 50MW gap in NSW.
- The nature of scheduled demand forecasting is already shifting away from a demand centred starting point to a weather-centred starting point, with all the complexity that it brings. The Reliability Panel has been made acutely aware of this dilemma through the recent Reliability Settings consultation in 2017/2018.
- When identifying the gap, it needs to be narrow enough to empower new technologies and demand response a real solution in demonstrating compliance. This will minimise over contracting and reduce the cost of compliance. Compliance methods should also be measured in line with the concepts of flexibility and dispatchability as per the AEMC's Reliability Frameworks Review.
- Whilst we support the AER as an independent entity, the above comments on resourcing remain.
- The Qualifying Contracts 'Option 5' requires significant work. We can foresee a situation where a large gentailer in a mid-sized region would prevent the MLO from being triggered through careful forward projections of additional supply, thereby preventing the trigger and the MLO and therefore, maintaining reduced liquidity and transparency.

The additional information on the role of demand response was welcome but still incomplete. The examples included in the 'TWP – Demand Response' require greater development down from yearly-like timeframes to weekly, predispatch and on the day (assuming various states of reliability triggers) – this is where the inherent price risk materialises and is dealt with a daily basis by participants such as Flow Power.

The inherent and underlying assumption that an ESOO-like process will be able to predict with any certainty in the future the likely gaps, especially given the increased amounts intermittent generation going forward, is flawed for the generation supply sector of the future. The times in the future when reliability and price standards will not be met will likely move away from peak summer/winter demand periods to periods where intermittent generation is low (no wind/little sun) and the dispatchable plant mix is inadequate (for whatever seemingly valid reason ie no gas, planned outages, no energy in storage etc). How this type of outcome is dealt with needs further, detailed assessment which Flow Power would be pleased to contribute.

Compliance and Penalties (4.8 / 4.9)

The spot pass-through business model employed by Flow Power appears problematic in the current context of the NEG design, despite its customer benefits and value, and the fact that customers on spot pass-through is not the problem being resolved by the NEG.

Whereas other retailers offer customers a fixed price (and manage the risk for them – at a premium), Flow Power has a high proportion of its customer base on spot price pass through arrangements, with many utilising demand response to manage price risk. In designing the NEG to take into account current market conventions and qualifying contracts, for other retailers, the purchase of swaps or caps for risk management purposes will also enable them to largely meet their reliability obligations in the event of a gap being identified. For Flow Power, the purchase of risk management products is not required to manage the price risk borne by customers, but the NEG will obligate us to purchase these products to meet reliability obligations. This will come at increased financial impost to our business.

Flow Power believes demand response is an effective method of managing spot price risk for a large proportion of our customer base as they are best placed to respond to price signals in managing cost outcomes. The price sensitive demand response is equivalent in nature to the implied supply response that a seller of swaps or caps in the market would make in defending their revenue position. As such, Flow Power is supportive of a high level of “firmness” being assigned to demand response products.

Demand response is an evolving product with increasing utilisation in the NEM, therefore we request further consideration for the above points in the final determination and future detailed policy specifications.

Examples where we see unresolved issues:

	UNDER ANOTHER FORM OF THE NEG	UNDER THE CURRENT FORM OF THE NEG
Scenario one: predicted high market event that eventuates	<ul style="list-style-type: none"> Spot exposed customers are informed of the event. They reduce demand on the system in response to the price. They avoid the higher power prices. The market price reduces and the customer benefits. 	<ul style="list-style-type: none"> Spot exposed customers are informed of the event. They have been contracted to meet the reliability obligation They take no action. The market price remains high and the customer pays the cost
Scenario two: predicted high market event that does not eventuate	<ul style="list-style-type: none"> Spot exposed customers are informed of the event. They get ready to reduce demand on the system in response to the price. No response is required No cost is incurred by the market or customer 	<ul style="list-style-type: none"> Spot exposed customers are informed of the event. They have been contracted to meet the reliability obligation They take no action. The market reduces but the customer still paid the

	UNDER ANOTHER FORM OF THE NEG	UNDER THE CURRENT FORM OF THE NEG
		higher price for the contract.