Energy Security Board

By email: info@esb.org.au

8 March 2018

**Re: Submission to the Energy Security Board's (ESB's) consultation paper on the draft design of the National Energy Guarantee (NEG)**

Spark Infrastructure welcomes the development of the NEG which will bring Australia's carbon and energy policy together and improve certainty for investment in the Australian energy sector. This will reduce pressure on the cost of capital to support a low cost, low emission, reliable energy system for all Australians.

Spark Infrastructure is listed on the Australian Stock Exchange (ASX) and is a leading Australian investor in Australian electricity transmission and distribution Network Service Providers (NSPs) who transport electricity to customers in South Australia, Victoria and NSW. We have a current market capitalisation of around $4 billion and our investment portfolio includes:

- 49% interest in SA Power Networks (electricity distribution in South Australia),
- 49% interest in CitiPower and Powercor (electricity distribution in Victoria, together known as Victoria Power Networks), and
- 15% interest in TransGrid (electricity transmission in NSW).

Spark Infrastructure and its investors are the providers of long-term equity capital into these NSPs which is necessary to build and maintain the networks required to deliver critical electricity to customers whilst maintaining the high standards of safety, reliability, security of supply and efficiency demanded by customers and regulators. These networks will be critical to supporting a changing mix of generation and distributed energy resources as the market evolves from thermal to renewable generation. We are very focussed on ensuring that our networks provide the services our customers require at least cost.

Domestic and global capital is highly liquid and is attracted by secure and robust investment destinations. Uncertainty in energy policy and critical infrastructure planning will see efficiently priced (lower cost) capital quickly relocate to alternate investment locations, whether that be alternate industries or countries.

Our response to the ESB's Draft Design Consultation Paper consultation paper is limited to the following issues:

1. Networks are critical to achieving the objectives of the scheme; interconnection opportunities must be considered on a level playing field
2. The new scheme must be demonstrated to be effective and deliver net benefits in relation to emissions, reliability and low-cost objectives
3. The important role of pricing reform to support objectives.

Further explanation of these issues is provided below.

## 1. Networks are critical to achieving the objectives of the scheme by ensuring interconnection opportunities are considered on a level playing field

Networks play a critical role in achieving the objectives of the NEG scheme. The changing energy market landscape is highlighting the importance of strategically located, efficient and reliable networks. The need for transmission development, previously driven by load growth, is now predominantly driven by the changing generation mix and the location of new generation. The transmission and distribution network spine will enable an

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orderly transition away from aging coal fired generation to geographically diversified and dispersed renewables and is the most effective way to enable peer to peer trading for residential and business customers.

The NEG must build on the strong regulatory framework for networks and interconnection. The current framework for economic regulation of NSPs encompasses important principles that provide strong incentives for efficiency to reduce the costs to customers. The regulatory framework also ensures these investments are scrutinised and deliver net benefits to customers. It is therefore important that the NEG scheme does not overlook or prevent network options or the supporting planning, governance and evaluation framework established for these investments. The NEG scheme will need to take in to account, and inform, the Integrated System Plan (ISP) being developed by the Australian Energy Market Operator (AEMO), the Distribution Market Model being developed by the Australian Energy Market Commission, and regulatory investment test (RIT) and Ring Fencing requirements being revised by the Australian Energy Regulator. Regardless of the specific outcomes of these reviews, investors in the sector need certainty that these will be developed as an integrated and supportive package.

Interconnection can be an alternative, substitute or facilitator for new generation and should be recognised in the gap analysis and response. To ensure that interconnection can be properly assessed against the reliability and cost objectives, it is important that interconnection opportunities are not unintentionally disadvantaged. This can be achieved by considering interconnection solutions in the design of reliability measures as well as any incentives (for example, direct payments or penalties and compliance and enforcement actions) for retailers. Further, the timelines and process should be consistent with the consideration of the ISP and RIT.

## 2. Ensuring the new scheme is effective and delivers net benefits in achieving the emissions, reliability and low-cost objectives

The design of the NEG scheme must consider both effectiveness and efficiency across all the segments in the electricity supply chain, i.e. Generation, transmission, distribution, retail and other innovations that may be introduced. We support the concept of the NEG scheme. However, there is the potential for the scheme to result in further costs being imposed on end-use customers with little demonstrable improvement in reliability or emissions. As an investor in network businesses in the Australian energy sector, we are acutely aware of the focus on affordability and consider that there should be a high bar set before additional costs are imposed on end users.

We see that these additional costs could include:

- The administration and assessment of individual contracts
- Delays in assessment and penalties that result in the procurer of last resort becoming the default option
- Socialising poor performance costs through the procurer of last resort
- Higher generation costs as market power is shifted from retailers to generators
- Bias against lower cost interconnection solutions because of barriers to participation or penalties and incentives that favour generation.

The design of the scheme should minimise administration costs whilst ensuring incentives consistent with desirable outcomes. The further work by the ESB should include a cost benefit assessment of the scheme compared to alternative options and testing of the schemes performance had it been in place during previous significant reliability events.

## 3. The Important role of pricing reform to support objectives.

We consider the NEG's value may be undermined if pricing reform is not accelerated. Electricity networks are being used increasingly differently by customers as electricity flows move from traditional one-way flows from centralised coal-fired baseload plants to multi-directional and net flows from new distributed and intermittent renewable generation sources. This fundamental change in the way customers engage with networks requires a new tariff charging paradigm, away from the largely volumetric basis that is used today. A change in network tariffs will result in a retailer response. The impact on customers will depend on the ability of the retailer to manage customer response.

Efficient tariffs signal to customers and investors the real cost of the network and the other components in the bundled electricity price and provide better information to compare the costs and benefits of different supply solutions. This can reduce the need to invest in building capacity, signal the need for additional generation and facilitate efficient adoption of emerging technology and behind the meter generation. Further, the full benefits of investment in advanced interval meters and peer to peer trading will only be delivered if efficient tariff structures are passed through to customers. In the absence of pricing reform to ensure a level playing field across the energy supply (and demand) sector, the NEG could result in additional investment which increases the overall cost of the system rather than reduces it.

We invite you to contact us to discuss this submission further or to seek further information. Please call Sally McMahon, Economic Regulatory Advisor, on 0421057821.

Yours sincerely,

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