



Energy Security Board
Submitted via email: info@esb.org.au

9 June 2021

Post 2025 Market Design Options Consultation Paper

BlueScope Steel Limited (**BlueScope**) welcomes the opportunity to provide a submission to the Energy Security Board (**ESB**) in response to the Post 2025 Market Design Options Consultation Paper dated 30 April 2021 (**the Consultation Paper**).

BlueScope is Australia's largest steel manufacturer and the only flat steel producer. We employ 6,200 people in Australian regions and cities to supply our nationwide customers in the building and construction, manufacturing, transport, and agriculture sectors. BlueScope also exports steel products and is a global leader in premium coated and painted steel products, manufacturing in 17 countries.

As a large user of electricity, BlueScope places great importance on both the cost of electricity and reliability of supply. Whilst this is important to all consumers, the scale of BlueScope's operations and the quantity of energy required mean that both cost and reliability issues have the potential to significantly impact BlueScope's business.

BlueScope appreciates the ongoing engagement and the commitment from the ESB to a comprehensive work program that seeks to facilitate an efficient, low emissions market that complies with the National Electricity Objective (NEO). Ensuring the market is fit for purpose both throughout and post the transition to a low emissions system is vitally important to large energy users who rely on affordable, reliable and sustainable supply to remain competitive.

Our key submissions in relation to the Consultation Paper, which are set out in more detail at Schedule 1, are based on the following high-level principles:

- 1. A national, consistent approach to market reform is fundamental to ensure affordable reliable electricity supply for customers:** We agree with the ESB's view that despite States having their own energy agenda there is an intricate link between energy generation and transmission and support the proposed coordinated approach to government underwriting schemes. The case for national coordination has never been stronger as a more intermittent and disperse generation system relies on locational diversity and strong jurisdictional interconnection to operate effectively. To the extent that investment signals are required, they should be focused on energy stability across the States in a way that best matches supply and demand across the NEM. A consistent national approach would also provide clarity and lower complexity for large users who operate across multiple NEM states.
- 2. Large users must maintain flexibility and optionality to best manage their costs:** The more out of market, directional, centrally procured services there are, the less leverage large energy users have to negotiate a favourable price outcome as these services are then largely deemed pass-through costs and non-negotiable. Therefore, BlueScope supports a market-based approach over mechanisms that utilise centralised procurement or regulated budgets (ie network tariffs).
- 3. Increased market transparency will benefit consumers:** We support increased levels of transparency of information relating to generator closures for the benefit of all market participants. Restricted access to

information makes it difficult for the market to respond to changing circumstances and increases the likelihood of more costly intervention and solutions.

4. **Reliability is important but not at any cost:** Recent capacity investment announcements have led us to question whether the RRO is required to incentivise investment in new generation. However, to the extent that the ESB considers that the RRO is required, we oppose any further reform to it and particularly oppose the introduction of physical certificates – which in our view is akin to the introduction of a capacity market and could unnecessarily increase the cost of reliability for consumers and large users in particular.
5. **Demand response is a critical element of a cost effective, secure and reliable electricity system:** BlueScope is a strong advocate for demand response as we believe it is a cost-effective way of reducing market volatility and ensuring system security and reliability. We encourage the further development of a demand response framework, including further consideration and development of 'scheduled lite', which recognises the range of demand response services which can be provided and goes some way to providing firm and transparent signals for demand response.
6. **Cost and risk associated with network transformation should not be assigned to customers alone:** While customers benefit from network investment, they are not the sole beneficiary, nor are they able to control the level of investment required as a result of new generation network requirements. We believe that given generators will benefit and have some control over the investment risk, they should also materially contribute to the cost of related network investment. This approach will not only be more equitable but also force new generation providers to think about the total cost of supply to consumers not just the most efficient generation location.

As a general comment, we are becoming increasingly concerned at the volume of reform in the market, and at times the disjointed approach being taken to energy reform. These proposals are complex and are increasingly – and rightly so – exploring demand-driven solutions, and as a large energy user it is vital that BlueScope advocates on the issues most relevant to it. Participating in the energy reform agenda is requiring increasingly greater levels of resources, which comes at a cost that cannot be passed on to BlueScope's own customers. We encourage the ESB to consider ways to ensure meaningful engagement by users and we query whether, in future, a dedicated 'consumer advocate' or similar role could be appointed to contribute to challenge reform options from the perspective of end users.

If further comment or clarification is required, please contact Bridgette Carter, Manager Energy Development on 02 4240 1749 or David Jenkins, Manager Government Relations on 03 9666 4022.

Yours sincerely



Bridgette Carter

Manager Energy Development

BlueScope Steel

Schedule 1 : Detailed Submissions

BlueScope's response to a number of the questions for consultation are set out in the table below. Our responses are guided by our key principles (set out above).

Item	BlueScope submission
A. National and Coordinated Approach	<p>We support the proposed co-ordinated approach to government underwriting schemes to help ensure that the investment driven by these schemes is better integrated with existing market design. We believe that a coordinated approach will provide clarity for investors and developers as well as less complexity for market participants. It should also lead to more efficient investment and, as a result, a lower cost of supply to consumers.</p>
B. Maintaining flexibility and optionality	<p>As a large user of electricity, BlueScope values the ability to effectively manage its own costs. Any proposals which have the effect of locking BlueScope in as a price-taker and removing flexibility to engage with relevant market participants dilute the value derived from our energy management approach and are strongly opposed. BlueScope is particularly opposed to any cost pass-through measures, which have the effect of costs becoming part of the regulated asset base of monopoly service providers.</p> <p>In this respect, the AEMC's draft determination on the <i>Efficient management of system strength on the power system</i> raises a number of issues for end users. We believe that the procurement model being proposed is likely to lead to a risk of over procurement.</p> <p>One reason for this is that the draft determination provides that AEMO's forecasting of specifications needs to be completed three years in advance, even though many renewables projects are planned and constructed within a two-year period. This mismatch in timing means that the forecasts made will lean towards over procurement so as to avoid the risk of a shortfall in system strength.</p> <p>Another reason the proposal is likely to lead to a risk of over procurement is that the methodology in the draft determination seems to assume that there is no system strength provision as part of the current business as usual operation of synchronous generators. Instead generators will be contracted for the provision of system strength, which could result in reduced prices in the energy only electricity spot market and diminish the value of long-term contracts executed by end users who will also likely pay for system strength as a pass-through cost.</p> <p>We believe that the cost of any over procurement should be passed down to generators. Generators are in a position to mitigate their costs in this respect, as they will be given a choice between paying the system strength charge or themselves remediating their general system strength impact. Our understanding of the draft rule is that security payments by generators will be ex-post in nature and as such if a generator has chosen to let the TNSP invest in system security measures to meet their forecast security obligations and consequently the generator self-remediates or the forecast security requirements are higher than the actual requirements, this cost will be worn by customers. We do not consider this to be acceptable and would urge the AEMC to review the mechanism to prevent</p>

Item BlueScope submission

consumers from directly paying for forecast inaccuracy and generator actions that minimise their own costs after committing the TNSP to expenditure for system security.

Proposed changes to the Retailer Reliability Obligation (**RRO**) which would result in an ongoing obligation in relation to reliability would increase costs to retailers and the composition of these costs will not be transparent for end users (e.g. an undefined liability period). Similarly, it is unclear how the cost of the proposed operational reserves market could be made transparent upfront unless a liquid hedging market of operational reserves is developed, something we consider to be unlikely. Our further submissions on the RRO are set out in more detail below.

C. Increase transparency in the market

BlueScope supports the provision of additional information being provided to governments and market participants in relation to future generator closures (including in relation to mothballing and seasonal shutdowns).

The provision of more information to the market will lead to positive outcomes for all market participants and will put the market in the best position to respond to future change, ideally without the need for government intervention. In relation to information provided around mothballing and seasonal shutdowns, we would also expect generators to provide detailed information on their capacity to come online. Information should be provided in a consistent manner. Agreed definitions should be established to ensure a consistent approach to the use of concepts such as 'mothballing' when they are used by reporting entities.

D. Retailer Reliability Obligation (**RRO**)

BlueScope has reservations as to whether there is still compelling evidence supporting the use of the RRO as a compliance mechanism to incentive investment in new generation. Market intervention should be a last resort and only where there has been clearly demonstrated failure by stakeholders to respond; in this case by investing in new, reliable energy investments.

Several market participants have recently progressed firming generation. For example, EnergyAustralia has committed to building Tallawarra B, AGL has committed to building a 250MW battery at Torrens Island in South Australia a battery is being developed at Darlington Point Solar Farm (as a result of a contract for the NSW government load). These examples demonstrate that the market is responding to an expected shortfall notwithstanding that the RRO has not been triggered.

Tallawarra B alone should cover the forecast reliability gap for 2023/2024, for the stricter interim reliability measure, noting that AEMO's assessment does not currently account for other confirmed projects, including Transgrid's 50MW battery at Wallgrove and the 50MW New England Solar Farm BESS. In addition, even though the 2020 Electricity Statement of Opportunity (**ESOO**) fails to identify any significant risks in reliability, Snowy Hydro is proceeding with its investment in the

Item BlueScope submission

Kurri Kurri peaking generator. Investment from both private and public sectors is occurring beyond any forecast reliability breach and in the absence of any trigger of the RRO.

Furthermore, recent events such as high spot prices in May 2021 in NSW in particular in the evening peak period resulting in a \$47.20/MWh cap payout for the month and an average cost for the most expensive hour of the day of nearly \$1,200/MWh, show peaking generation can be valued under current market rules when the supply/demand balance is tight. The relatively limited valuation of peaking generation is likely reflective of the reasonably well-supplied market exhibited in the 2020 ES00, not necessarily a market lacking price signals. It should also be noted that forward market prices in New South Wales in particular have recovered significantly from early April 2021 lows of around \$50/MWh and should be close to, if not over, the long-term cost of existing coal-fired generation at \$57/MWh.

We also note that the current T-3 trigger does not facilitate investment in projects such as pumped hydro, which require much longer lead times to plan and construct – meaning that the RRO is arguably not achieving its stated aim in any event.

As a large user, we are also concerned that the RRO and proposed changes to bolster compliance will disincentivise timely and efficient responses to reliability shortfalls via demand response as the mechanism requires market participants to be firmly contracted when the RRO is triggered. These contracts will likely cover periods greater than required to cover the perceived reliability gap that will likely lead to unnecessary cost being worn by large users (e.g. a quarterly contract to cover a shortfall that is forecast only in January and February would result in consumers needlessly paying for coverage in March).

To the extent that the RRO is maintained we strongly oppose any further amendment to it. Given its infancy, we consider that any amendments will contribute to uncertainty in the market, undermining confidence for private investment. If the RRO is to be retained, it should be given time to work in its current form.

We do not agree that the reasons given in the Consultation Paper as justification for a proposed change to the RRO are borne out in the market. For example, it is unclear how the RRO stops sudden closures of generators, which is most likely to occur due to catastrophic failure. Secondly, the notice of closure requirements is already in place with the aim of stopping sudden closures. To the extent this outcome is not being achieved then it would be preferable to address this issue directly instead of amending the RRO. For example, we consider that the reforms around increased transparency in the market would mitigate the risk of sudden closures of generators. We are particularly opposed to a physical RRO. In our view, this is in effect a capacity market which benefits large generators. In giving effect to a de-facto capacity market, the changes to the RRO may also impact on the value of long-term contracts as value is likely to be removed from the energy-only spot market which supports returns to those projects. In effect, given the need for such changes is arguable at best, making these proposed changes increases regulatory risk and may in fact increase barriers to investment in the NEM and disincentivise long-term contracting.

The proposed RRO changes also appear to operate in isolation to broader drivers for investment, most notably increasing ESG pressure on major energy companies to take meaningful climate change action. Energy generators must balance pure economic investment signals with the need to be responsive to climate change concerns. The announcement by AGL on 8 June 2021 of its intention to construct a concentrated solar thermal facility on the site of the Liddell coal-fired power station is evidence of this. Although the investment is for a much smaller volume of electricity it is a demonstration of a transition towards investment that responds more to climate change signals.

Item BlueScope submission

E. Demand response

BlueScope is a strong advocate of demand response and supports the exploration of the scheduled lite proposal and its stated objectives.

BlueScope agrees that the scheduled lite design should not require onerous or excessive information that does not deliver value to the market operator or broader market, and that the design should try to balance the risks and obligations with the incentives to participate. To ensure the scheduled lite proposal delivers on these key design principles and maximises participation to improve the overall benefits of the reform, the following should be considered:

- The value proposition for individual participants must be clear and transparent, so that users can effectively assess the financial benefits of participation. The incentives described in both scheduled lite models do not deliver price certainty when participation decisions are being made.
- Forecasting consumption for large electricity users can be challenging as unlike generators, industrial loads can vary from minute to minute due to the variable nature of production processes. A flexible and pragmatic approach that caters for variable loads when forecasting and determining forecast accuracy will be required to facilitate participation of large industrial users such as BlueScope. The application of non-financial consequences for inaccurate forecasts (such as reputational damage) under the visibility model is a significant deterrent to participation; the proposal that a participant be removed from the scheduling category if the accuracy threshold is breached without sufficient rationale is more appropriate.
- The requirement to provide granular (5 minute) and frequent bids into the pre-dispatch energy market under the dispatchability model will be resource intensive and onerous for large users whose focus is to conduct their core business activities rather than be energy traders. Further, large users with variable loads may be unable to participate in a market that requires 5 minute bids and settlements as they may struggle to curtail consistently to meet their short duration dispatch targets and the demand response activation leads times and durations may be too short to make participation worthwhile. Alternative options for bidding granularity and frequency would make the dispatchability model more attractive to large users.
- Further clarity is required around how obligations arising from participation in scheduled lite will be managed via contractual arrangements with Financially Responsible Market Participants (**FRMP**), such that consumers will not be required to directly interact with the market. This approach could see FRMPs dilute the benefits of demand side participation for the users; this would need to be addressed in future scheduled lite development activities.

BlueScope is strongly opposed to the proposed rule change to classify 5-30MW generators as scheduled (or semi scheduled) generators and consider the utilisation of demand response via scheduled lite as a more appropriate option to improve visibility of smaller generators. This rule change will likely disincentive large users from investing in co-generation projects that would have an overall positive impact on grid stability and carbon abatement as meeting the schedule generation obligations would be inefficient, costly and onerous.

Item BlueScope submission

F. Other – Ramping Capacity & Operating Reserves

We disagree with the ESB that ramping and operating reserve resources are not presently valued by the market. Our view is that they are already afforded their real value at any point in time given that:

- generators with ramping capacity or operating reserves are already rewarded during periods of market volatility through a higher spot price (in fact, ramping constraints do at times trigger spot price volatility when lower-priced capacity is available but unable or unwilling, based on its offered ramp rate, to meet the required ramp rate to balance supply and demand); and
- generators are incentivised to be ready to ramp to meet their obligations under their existing contracts.

In this sense, we consider that a separate reserve service would mean that generators are 'double dipping' in that they are being paid the spot price and / or under their contracts, as well as being paid a fee for providing a reserve service.

We also consider that demand response has the potential to significantly reduce the need for a reserve service. Having both a demand response mechanism and a reserve service means that generators may be paid for a service which may be redundant in circumstances where users are better placed to respond.