THE HON JOSH FRYDENBERG MP
MINISTER FOR THE ENVIRONMENT AND ENERGY

PDR: MC17-019899

Dr Kerry Schott AO
Chair, Energy Security Board
Level 26, 1 Bligh Street
SYDNEY NSW 2000

Dear Dr Schott

I am writing to request the Energy Security Board (ESB) undertake further work, building on your previous analyses of the proposed National Energy Guarantee in the National Electricity Market (NEM), including electricity market modelling.

The ESB provided advice to the Commonwealth Government at our request on 13 October 2017. This advice proposed a National Energy Guarantee to achieve a more affordable and reliable electricity system while helping to meet Australia's international commitments to reduce emissions. The proposal aimed to deliver on the Chief Scientist's recommendations by focussing on their implementation.

I thank the ESB for its advice about the security and reliability of the NEM and for its work in developing the National Energy Guarantee proposal. The Government appreciates that the proposed design of the mechanism will minimise disruption to the current market rules and arrangements, provide participants with the time and flexibility to meet the desired outcomes, and increase certainty in the NEM to promote greater and more efficient investment.

Building on previous analyses, I request the ESB undertake detailed electricity market modelling based on the attached criteria and provide a report on the findings from this exercise to the Government by 13 November 2017. The Government has indicated it will share the modelling results with the COAG Energy Council. The Government will provide the necessary funding to the Australian Energy Market Commission to enable this work to be completed. The ESB should also provide a report to the Government on the operation of the National Energy Guarantee and its impacts on the NEM. The report should assess the mechanism in terms of its ability to improve energy affordability and reliability while reducing emissions.

I look forward to continuing to ensure Australia's electricity supply remains affordable, secure and reliable, and continues to contribute to meeting Australia's international commitments.

Yours sincerely

JOSH FRYDENBERG

Attachment: National Energy Guarantee Modelling Scenario

The modelling should reflect the two key parameters of the National Energy Guarantee:

- the Australian Government's commitment to deliver reliable electricity by ensuring sufficient dispatchable capacity is available in every region of the National Electricity Market (NEM) to meet peak demand; and
- the commitment by the Government to meet our international emission obligations.

The scope of the modelling is the NEM only, covering the period from 2020 onward noting that the reliability and emissions guarantee will be in place from 2019 and 2020 respectively. The exercise should include a business-as-usual (BAU) scenario, and a scenario implementing the National Energy Guarantee.

The emissions reduction target should be based on a least cost trajectory and assume a 26 per cent reduction on NEM emissions in 2005 by 2030, consistent with an emissions budget based on a linear trajectory from BAU emissions in 2020 to the target in 2030 – noting that this will be a policy decision for the Government. An example of an optimised non-linear trajectory that met the same emissions budget would be of assistance. The modelling should also assume a constant target post-2030.

The modelling should also include sensitivities for higher and lower than expected electricity demand, higher and lower than expected gas prices, and higher and lower than expected technology costs. The exercise may also include any further scenarios or sensitivities that could, in the Energy Security Board's view, provide the Government with valuable insights on the National Energy Guarantee.

In undertaking this exercise, the Energy Security Board should take account of other Government policies expected to impact on the NEM including, but not limited to, the proposed expansion of Snowy Hydro.

The modelling results should include the impact of the National Energy Guarantee on retail and wholesale electricity prices, as well as the expected generation and capacity mix compared to BAU. This information should also be provided on a state by state basis.

The outcomes for the National Energy Guarantee should be compared against previous modelling of climate and energy policies by the Australian Energy Market Commission.