

Should the ESB continue post 2021?

1. SUMMARY

Before the establishment of the ESB, best-practice NEM governance was in place whereby AEMO, AEMC and the AER each had separate functions providing confidence for investors and consumers in the roles and responsibilities of each body.

However, concerns were raised in The Finkel Review about reform delays due to the institutional discord between the Australian Energy Market Operator (AEMO) and the Australian Energy Market Commission (AEMC).

To address this discord, the Energy Security Board (ESB) was established comprising the heads of each of the three market bodies and an independent chair and deputy chair to deliver on four key outcomes of the Finkel Review: increased security, future reliability, rewarding consumers and lower emissions.

The industry has agreed that the ESB have accomplished what it set out to do in terms of addressing the discord between AEMO and the AEMC and have delivered a significant body of work overseeing the implementation of the Finkel recommendations and coordination of policy relating to energy security and reliability in the NEM.

With the lack of a national emissions policy, the states have filled the policy vacuum setting net zero targets and policies to support the development of critical transmission infrastructure and the uptake of renewable energy as the fleet of coal-fired generators retire. And the Federal Government have extended the life of ARENA by providing additional funding as the market eagerly waits for more details on the Technology Investment Roadmap.

In parallel with the ESB's body of work, AEMO has been progressing major reform on the Integrated System Plan and update to its renewables integration study whilst the AEMC continued in its role to consider rule changes put forward by market proponents.

Both the AEMC and AEMO now have new leadership and have signalled the importance of collaboration between the two organisations. This provides stakeholders with greater confidence in returning to the original governance structure where the AEMC and AEMO have defined roles no longer requiring the oversights and coordination of the ESB.

The ESB's sole workstream, the Post 2025 Market Design project, has been presented to Ministers with final decisions at a Ministers' meeting currently scheduled for September. This is approximately the same time that the Chair of the ESB, Kerry Schott, is contracted until and has announced her plans to exit before the ESB Secretariat funding runs out at the end of 2021.

We are calling on the state energy ministers to consider an alternative recommendation to the ESB in their next National Energy Cabinet meeting scheduled in September where the ongoing role of the ESB will be discussed:

- **An orderly wind up of the ESB upon completion of the P2025 report. This would see it close in approximately December 2021.**
- **A revised Statement of Role for AEMO and the AEMC addressing the roles in the provision of policy and market development advice.**
- **Institute a Market Bodies Forum (MBF) that gives energy ministers a singular forum to engage with the heads of the market bodies on policy and reforms needed with AEMC as secretariat.**

2. WHY THE ESB WAS FORMED

The South Australian state-wide blackout in 2016 created intense pressures on the states and highlighted the security of the National Electricity Market (NEM). In response, energy ministers announced the commencement of the Finkel Review, which considered the energy system, market and governance framework.

The Finkel Review, completed in 2017, raised concerns about *institutional discord between Australian Energy Market Operator (AEMO) and the Australian Energy Market Commission (AEMC), resulting in reform delays*¹.

One of the Finkel Panel's key recommendations to address this discord was to create the Energy Security Board (ESB), comprising the heads of the market bodies and an independent chair and deputy chair. The ESB was to remain in place until 2020 to implement the other 49 (of 50) recommendations.

The ESB was quickly established, appointments made, and it was given the power to directly make rules under the National Electricity Law (NEL) Section 90F.

This power was a radical shift as it allowed the Federal Energy Minister to direct rule changes via the ESB, instead of the established process where the Australian Energy Market Commission had sole custody of the rules. This new power effectively enshrined ministerial intervention in market rules and policy.

The ESB soon departed from the Finkel recommendations, with ministers directing the ESB to:

- Develop the National Energy Guarantee, that subsequently became the Retail Reliability Obligation (RRO)
- Review the transmission rules to simplify Integrated System Plan (ISP) planning
- Undertake the Post 2025 Market Design project (P2025 project), and
- Implement an interim Reliability Standard.

The National Energy Guarantee was abandoned and, after introducing the Retail Reliability Obligation, the ESB focused on a single workstream, the P2025 project, rolling in all other tasks.

3. POLITICS, GOVERNANCE, COORDINATION AND THE ROLE OF INDIVIDUAL MARKET BODIES

While the ESB was being established to respond to the discord between AEMO and AEMC, Ministers and Prime Ministers came and went over their views for or against action on climate change and reforms in the energy market. In light of this political inertia, it is not surprising that both Labor and Liberal state governments began to pursue policy and market reforms to secure their own energy and climate futures.

Lack of federal leadership and state-centric policy meant it was very difficult at that time to progress reforms and enhancements to the NEM that could have, in part, addressed the concerns of state energy ministers.

¹ Finkel Panel, *Independent review into the Future Security of the National Electricity Market*, p. 165.

Far from being addressed by the introduction of the ESB, these difficulties continue and are now largely embedded in the governance structure and opaqueness over roles.

Historical reviews of energy governance

The original NEM governance intentionally separated the functions of:

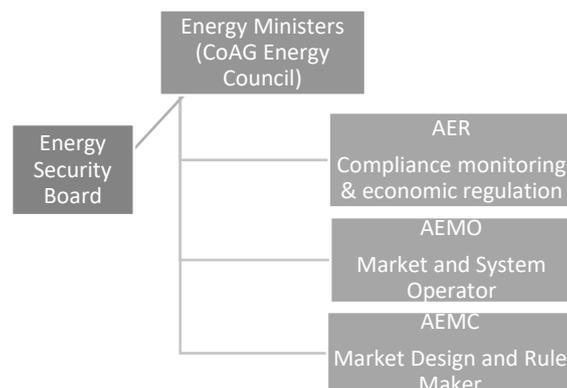
- economic regulation and enforcement in the Australian Energy Regulator;
- market and system operation in the AEMO; and
- market design and rule-making in the AEMC.

This separation represented best-practice governance², providing confidence for investors and consumers in the roles and responsibilities of each body.

Several reviews initiated by the COAG Energy Council have considered energy governance and made recommendations regarding what they consider to be best practice.

In 2015, the Vertigan Review³ recommended retention of the (original) governance structure, with suggestions to expedite the rule change process, and to *clarify AEMO's role*, particularly with respect to market design. Vertigan's recommendations were never implemented.

In 2017, the Finkel Review⁴ also documented concern about institutional discord and reform slowness. Taking a different tack than Vertigan, Finkel recommended creation of an ESB, in which the heads of the AER, AEMC and AEMO would sit alongside an independent chair and deputy chair. The Finkel recommendations were partially implemented before the role of the ESB was re-oriented. The creation of the ESB has led to our current governance structure:



² [Review of Governance Arrangements for Australian Energy Markets - Final Report - October 2015 \(energyministers.gov.au\)](https://energyministers.gov.au/publications/review-governance-arrangements-australian-energy-markets-final-report)

³ <https://energyministers.gov.au/publications/review-governance-arrangements-australian-energy-markets-final-report>

⁴ <https://www.energy.gov.au/government-priorities/energy-markets/independent-review-future-security-national-electricity-market>

In mid-2020, the Edwards Review⁵ considered the long-term role of the ESB. Edwards recommended the ESB continue until the end of 2021 to complete the P2025, which was accepted by Ministers. Edwards recommended disempowering S90F (this recommendation was rejected by energy ministers) and completing AEMO's statement of role (agreed, but not yet actioned).

Common findings across these reviews were:

- Clarity of roles between the AEMC and AEMO is needed for clear accountability and coordination and long-term certainty. It is acknowledged that the AER as a regulator has no role in policy development due to the conflict of interest between regulation compliance and good policy.
- The specific purpose of the ESB and its role need not be extended beyond 2021.
- Having a separate process for making rules (i.e. S90F) creates uncertainty and a pathway for government intervention. It is preferable to have a single, transparent rule change process.

4. WHAT HAS THE ESB DELIVERED AND WHAT HAS HAPPENED IN PARALLEL (VIA OTHER MARKET BODIES)

The ESB was created in highly political circumstances and had a 'tough ask' to coordinate reforms across market bodies. In this critical decade for action on climate change, its contributions should be assessed on whether the ESB will decarbonise the energy system at an accelerated pace with considerations to reliability, security, and affordability.

With that in mind, while the ESB has achieved partial implementation of the RRO (one of the Finkel Review recommendations), tightened the reliability standard (CoAG request), created actionable ISP rules (with AEMO) and developed Stage 1 Renewable Energy Zone (REZ) rules (CoAG request), it is important to note that the majority of effort and resources came from AEMO and the AEMC. ESB Chair Kerry Schott also submitted a request to the AEMC to require generators to provide three years of notice prior to closing a plant (originally a Finkel recommendation).

Meanwhile, the AEMC has continued in its role to consider rule changes put forward by market proponents and progressed reforms.

Box 1: Rule Changes & Market Reforms worked on by AEMC in parallel with ESB work program

- Streamlining the participation of storage in connecting to the NEM and participating in markets
- Fast frequency response and operating reserve markets development
- Primary frequency response for grid stability from large generators
- System strength framework for high renewables zones
- Project development and grid connection transparency reforms
- Wholesale demand response mechanism allowing DR aggregators to participate in the wholesale market
- Enhancing the transparency and structure of the reliability and emergency reserve trader (RERT) mechanism.

⁵ <https://energyministers.gov.au/review-energy-security-board>

Elsewhere, under new leadership, AEMO progressed major reform on the Integrated System Plan (ISP) and updated its renewables integration study.

The states have taken up the central policy void by establishing clear ambitions for net zero by 2050 and backing this up through reforming renewable energy-oriented policies, plans and investment settings.

Table 1: NEM States Transmission Initiatives

Government	Initiatives
<i>NSW Government</i>	NSW Government has developed an Electricity Strategy ⁶ and Electricity Infrastructure Roadmap ⁷ which sets out a plan to deliver the State's first five REZs as well as developing the NSW Transmission Infrastructure Roadmap ⁸ with the support of the Federal Government ⁹
<i>Victorian Government</i>	The Victorian Government are supporting the development of REZs ¹⁰ , the Western Victorian Transmission Network Project ¹¹ and Victoria-NSW Interconnector project.
<i>Queensland Government</i>	Queensland Government are establishing three REZs ¹² and supporting the development of CopperString 2.0 and the Queensland-NSW Interconnector (QNI)
<i>South Australian Government</i>	The South Australian Government are supporting project EnergyConnect which will open up renewable energy zones with support from the Federal Government ¹³
<i>Tasmanian Government</i>	The Tasmanian Government have developed a draft renewable energy coordination framework which includes proposed Renewable Energy Zones ¹⁴ and are developing the Marinus Link ¹⁵

While the key role for the ESB formation was to coordinate the reforms across the market bodies, there remains a lack of clarity and limited coordination between them and the ESB, with the industry still beset by multiple regulatory reviews and rule change processes underway.

⁶ [NSW - Electricity Strategy](#)

⁷ [NSW Government's Electricity Infrastructure Roadmap](#)

⁸ [NSW - Transmission Infrastructure Strategy](#)

⁹ [NSW - MoU](#)

¹⁰ [The Victorian Government is developing Victoria's Renewable Energy Zones \(REZs\)](#)

¹¹ [West Vict NP](#)

¹² [Qld - Renewable Energy Zones](#)

¹³ [Ministers Taylor Media Releases - South Australia](#)

¹⁴ [Draft Renewable Energy Coordination Framework](#)

¹⁵ [Marinus Link](#)

5. WHAT HAS CHANGED OVER THE PAST 4 YEARS SINCE THE CREATION OF THE ESB?

The Federal Government focus on technology as the States push the decarbonisation agenda

The Federal Government, as part of their Technology Investment Roadmap, have provided a lifeline to the Australian Renewable Energy Agency (ARENA) through additional funding that will drive private investment in technology to decarbonise the economy over this critical decade.

In the continued absence of federal energy policy, the states and territories took the lead in 2020, introducing a range of ambitious policies to accelerate Australia's renewable energy transition. Most positively, these policies occurred across the political divide, with both Liberal and Labor governments making strong commitments¹⁶ to renewable energy and decarbonisation. This is already having a noticeable impact on the electricity system, with many states and territories setting records for renewable generation throughout the year. The proportion of renewable energy in almost every state and territory has increased significantly.

The states are also looking at implementing governance structures such as VIC Grid¹⁷ and the (NSW) Consumer Trustee¹⁸, to deliver on these policies as the challenges and risks facing the states are present and real.

Change in leadership at AEMO and AEMC

Both the AEMC and AEMO have welcomed change in leadership over the past 12 months. At the AEMC, Anna Collyer has replaced John Pierce as Chair, who stood down from his 10-year post in June 2021.

There is broad support across the energy industry for the appointment of Anna Collyer due to her previous experience with energy law, active involvement in energy market reforms and experience with supporting innovation. Her appointment is seen as an opportunity for the AEMC to embrace faster reforms and keep pace with the accelerating transformation of Australia's energy sector.¹⁹

Daniel Westerman has replaced Audrey Zibelman as CEO of AEMO in what has been viewed as another positive move. Westerman brings the commercial, technical and regulatory experience to lead AEMO through significant change in the energy market. In his first speech since taking up the role in mid-May²⁰, he called for greater stakeholder collaboration with industry encouraged by Westerman's leadership:

"In order to maximise the benefits of this energy transition for the whole of society, all of us need to play our role and work collaboratively, together, and learn from one another; Committing us (AEMO) to greater openness, transparency and accountability for the interactions we have with all our stakeholders as we go about our work" Daniel Westerman, CEO of AEMO

Both Ms Collyer and Mr Westerman have signalled the importance of collaboration between the AEMC and AEMO. This provides stakeholders with greater confidence in returning to the original governance structure where the AEMC and AEMO had defined roles and the ESB was not required.

¹⁶ [clean-energy-australia-report-2021.pdf \(cleanenergycouncil.org.au\)](https://www.cleanenergyCouncil.org.au/clean-energy-australia-report-2021.pdf)

¹⁷ <https://www.energy.vic.gov.au/renewable-energy/renewable-energy-zones>

¹⁸ <https://www.environment.nsw.gov.au/news/new-electricity-consumer-trustee-to-put-energy-consumers-first>

¹⁹ [New AEMC chair - a head of innovation - to embrace rapid market transformation | RenewEconomy](#)

²⁰ [AEMO | AEMO CEO Daniel Westerman's CEDA keynote address: 'A view from the control room'](#)

6. CONCLUSION

In the aftermath of the South Australian black system event, the Finkel Review created the ESB to expedite certain critical changes, but in doing so blurred the important functional boundaries of the market bodies. Now that the Finkel Review's implementation period is complete, it is worth reconsidering whether the remaining value of the ESB exceeds the detraction from the original tri-institutional model.

With the new institutional leadership, a functioning policy and reform process coordinated through the state energy ministers and consistent policy agendas towards net zero emissions targets, this begs the question of the ongoing role (and cost) of continuing the ESB.

WIND UP OF THE ESB UPON COMPLETION OF THE P2025 REPORT

The recommendations of the Edwards review appear to largely align with previous views expressed by many stakeholder submissions which we endorse as a forward approach.

These include:

Box 2: Recommendations

- 1) *An orderly wind up of the ESB upon completion of the P2025 report. This would see it close in approximately December 2021.*
- 2) *A revised Statement of Role for AEMO and the AEMC addressing the roles in the provision of policy and market development advice.*

COORDINATION OF THE MARKET BODIES BEYOND THE ESB

Essentially the majority of effort by the ESB has been achieved through shared resources from AEMO and the AEMC. This makes the handover of any ESB ongoing initiatives seamless. To improve coordination between the market bodies to provide a single, authoritative source of reporting and coordinated advice without a statutory role can be achieved through a Market Bodies Forum (MBF). The concept was recommended by the Edwards Review and has been supported by majority of Industry and stakeholders. The MBF can play a key role in coordinating the market reform decarbonisation agenda and reforms needed including response to emerging issues and trends by utilising all mechanisms and powers available to its members and assist ministers in delivering the regulation and policy agendas in an open and transparent manner.

Box 3: Recommendation

- 3) *Institute a Market Bodies Forum that gives energy ministers a singular forum to engage with the heads of the market bodies on policy; where the AEMC provides the chair and secretariat; Senior Energy Officials to be represented to give government clarity as well as industry. Senior officials should be responsible for working with the market bodies and Industry to develop this forum.*

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