PROPOSED DEFERRAL OF NETWORK CHARGES RULE CHANGE

MICHAEL BRADLEY, EGM – AEMC

BEN DAVIS, DIRECTOR – AEMC

MITCH SHANNON, SENIOR ADVISER – AEMC

AEMC

Agenda

1. Introduction
   Ben Davis – Director, AEMC
2. The rule change rationale, scope and key issues
   Mitch Shannon – Senior Adviser, AEMC
3. The rule change process
   Mitch Shannon – Senior Adviser, AEMC
4. Questions
5. Next steps – conclusion

Purpose of today’s forum

- The rule change process will consider whether to introduce a deferral mechanism for the payment of network charges by retailers.
- Today’s workshop will outline the AEMC's approach to the rule change process and our key questions in the Consultation paper to inform stakeholders in preparing submissions.
- If you would like to organise a meeting with the AEMC to discuss, please contact the project team.

THE RULE CHANGE RATIONALE SCOPE AND KEY ISSUES

Rule change request and rationale

On 6 May 2020, the AER submitted a rule change proposal seeking to allow retailers to defer the payment of network charges for customers impacted by COVID-19 for six months. The deferral would apply to network charges incurred between 1 July and 31 December 2020.

Rationale

- Submitted in response to the potential impact of COVID-19 on retailer cash flows.

- Allowing retailers to defer these payments will allow them to prioritise supporting vulnerable customers and enhance the financial resilience of the energy industry in the short-term, as this would provide cash flow relief which reduces the risk of multiple retailer failures.

Scope of rule change

- Scope is confined to the specific issues raised in the rule change request.
- The Commission will consider whether allowing retailers to defer the payment of some network charges is necessary to support financial resilience and preserve an appropriate level of competition in the retail market, given the impacts of COVID-19.
- If the Commission deems the deferral mechanism necessary, a number of design issues would need to be considered. These are addressed in the consultation paper and will be discussed in today’s forum.

Applying the National Electricity Objective (NEO)

Commission may only make a rule if it is satisfied that the rule will, or is likely to, contribute to the achievement of the NEO:

to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to

a) price, quality, safety, reliability and security of supply of electricity; and

b) the reliability, safety and security of the national electricity system.

Commission will assess the rule change request against the criteria in the assessment framework, which includes:

Promoting financial resilience – would the proposal support industry viability and financial resilience by deferring costs for retailers facing cash flow risks as a result of the COVID-19 pandemic?

Efficient allocation of risk – would the proposal appropriately allocate any associated risk and cost to the parties best placed to manage them?

Implementation costs – costs should be minimised relative to the benefits of the proposed deferral mechanism.

Key issues and questions to consider

- Impact of COVID-19 on retailers
- Coverage of the deferral mechanism
- Deferral timeframe and terms
- Deferral of payments between DNSPs and TNSPs
- Practical implementation of payment deferrals
- Impact on NSPs

Impact of COVID-19 on retailers

Key questions

- How COVID-19 has impacted retailers’ cash flows?
- What options are available to retailers to manage the cash flow impacts of COVID-19?
- How would the proposed deferral mechanism impact retailers’ cash flows?

Considerations

- COVID-19 is expected to continue to impact on retailers’ cash flows in the short-term, with the potential for some lag effect in the manifestation of these impacts.
- Some retailers may be able to secure additional funds to address these cash flow issues.
- A number of support schemes have already been announced or implemented by governments and network businesses – is further financial assistance necessary?

Coverage of the deferral mechanism – retailers

Key questions

- Is it appropriate to expressly exclude certain classes of retailer from deferring the payment of network charges?
- What eligibility criteria and verification process should apply to retailers seeking to access the mechanism?
- Should financial incentives (e.g. interest on deferred payments) be used to influence which retailers seek to access the mechanism?

Considerations

- It is appropriate to consider limiting access to the proposed deferral mechanism to retailers that have a demonstrable need for this support as a direct result of COVID-19.
- This would affect the materiality of the cash-flow burden that DNSPs are required to take on.
- The approach taken should be capable of being administered efficiently to ensure timely access to payment deferrals.

Coverage of the deferral mechanism – customers

Key Question

- Which customers should be captured by the proposed deferral mechanism? Should this include large customers?
- Are new payment plan and hardship customers the appropriate small customers to include in the mechanism?

Considerations

- The AER's Statement of Expectations does not restrict retailers from disconnecting large customers for non-payment (except where that customer is on-selling energy).
- Retailers are more likely to hold security which they can draw on in the event of non-payment by large customers.
- The existing Network Relief Package only applies to residential and small business customers.

Deferral timeframes and terms

Key questions

- Is a six-month deferral period appropriate, having regard to the potential cash flow impacts of COVID-19 in the second half of 2020?
- Would a shorter deferral timeframe be sufficient to allow retailers to overcome the financial pressures posed by the current environment?
- Is it appropriate for the AER to have the ability to extend the deferral period if necessary?

Considerations

- Current indications are that the adverse impacts on the Australian economy, including increased unemployment, will continue to be felt through to the end of 2021.
- If the AER were to have the ability to extend the deferral period, it would be important that any such decision be based on consideration of the circumstances of market participants and the extent to which the deferral mechanism is still necessary.

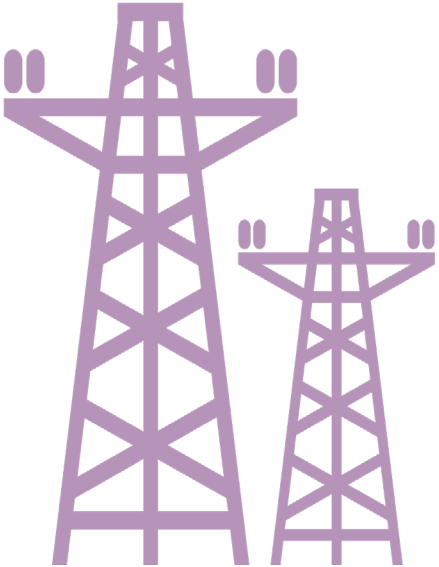
Deferral of payments between DNSPs and TNSPs

Key questions

- Is it necessary for DNSPs to be able to defer the payment of some transmission charges to TNSPs?
- How could the deferral of payments from DNSPs to TNSPs be implemented in practice?
- What issues would need to be addressed in the regulatory framework to facilitate this?

Considerations

- This is a complex issue which may require consideration of a range of policy issues and potentially substantive changes to the NER to implement.



Practical implementation of payment deferrals

Key questions

- What processes could be adopted to facilitate the proposed payment deferrals in an expedient manner?
- Could the processes agreed between retailers and NSPs for implementing the Network Relief Package also be used to implement the AER's proposal?
- Is it feasible for the details of this process to be directly agreed between NSPs and retailers?

Considerations

- It would be important to ensure that retailers and DNSPs are able to identify eligible retailers and/or customers and agree on payment deferrals for those customers using a clear and efficient process to reduce the scope for disputes or miscommunication.
- While the NER may include high-level principles relating to the deferral process, it is unlikely to be practical for the details of this process to be comprehensively set out in the NER.

Impact on NSPs

Key questions

- Would a six-month deferral of the payment of network charges pose a material financial risk to NSPs and, if so, are there ways of addressing these risks through the design of the mechanism?
- Would the annual pricing proposal process allow NSPs to recover any deferred revenue in the following regulatory year?
- What would be the best mechanism to reimburse NSPs for the direct costs incurred as a result of the deferred payments?
- If NSPs were to be reimbursed for their efficient costs (as well as recovering their total regulated revenue), would there be any residual risk to their business?

Considerations

- NSPs would remain entitled to recover the full amount of revenue determined by the AER under its regulatory determinations.
- The Commission acknowledges that the proposed deferral mechanism would have an impact on NSPs' cash flows in the short-term.
- There may be an assumption that efficient network businesses should be able to secure additional credit to manage these cash flow impacts if needed.

THE RULE CHANGE PROCESS

Request for an expedited rule change process

AER's proposal
The AER proposed that the rule change request be treated as an urgent rule and processed on an expedited basis.

AER’s reasons
The AER’s request was made on the basis that, if the rule change request was not made as a matter of urgency, it may imminently prejudice or threaten the effective operation and administration of the wholesale electricity market or the safety, security and reliability of the interconnected electricity system.

The AER suggested the impacts of COVID-19 necessitate the request being treated as an urgent rule.

In particular, the AER suggested the financial resilience of the industry is being threatened because electricity retailers are facing an imminent risk of incurring ongoing costs without matching revenue streams to meet those costs as a result of the impact of the pandemic on customers' ability to pay their power bills.

Commission's reasons to apply an expedited rule change process

Commission's decision
The Commission considered that the rule change should be subject to an expedited rule making process.

Commission's reasons
The economic impact of COVID-19 threatens the financial viability of retailers and potentially the financial resilience of the retail market more broadly. These impacts could be reduced if a decision on the AER’s proposal is made as soon as possible.

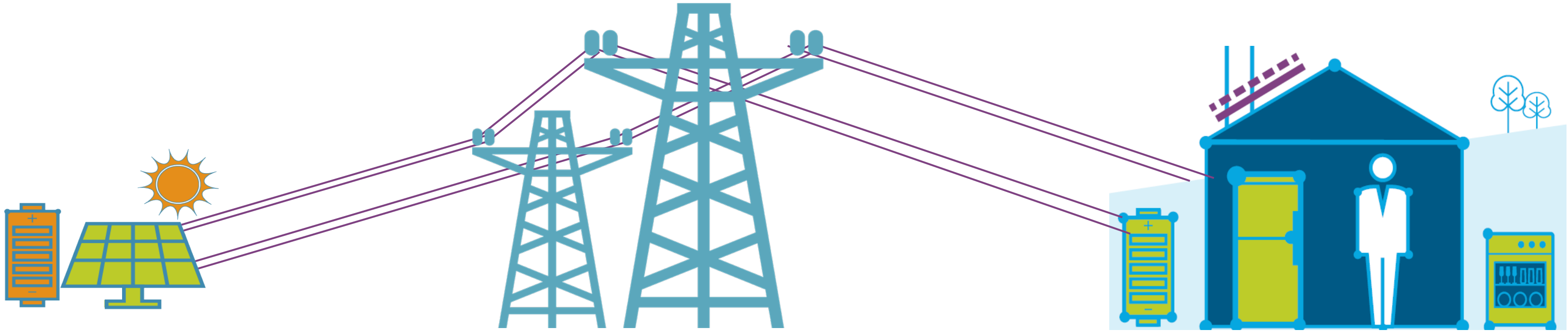
- The COVID-19 pandemic has caused a severe economic downturn and there has been a material decrease in total wages and increase in unemployment.
- The potential for a material reduction in incoming cash flows may cause financial stress for retailers and could lead to financial contagion in the retail market.
- The design of the RoLR scheme does not provide the flexibility required to manage the impacts on the retail market of successive retailer failures in the short term
- The failure of multiple retailers in the short-term is likely to have negative long-term impacts on competition in the retail market.
- The purpose of the AER’s proposal would be undermined if the rule change were subject to the standard rule-making process.

Timeline for this expedited rule change process

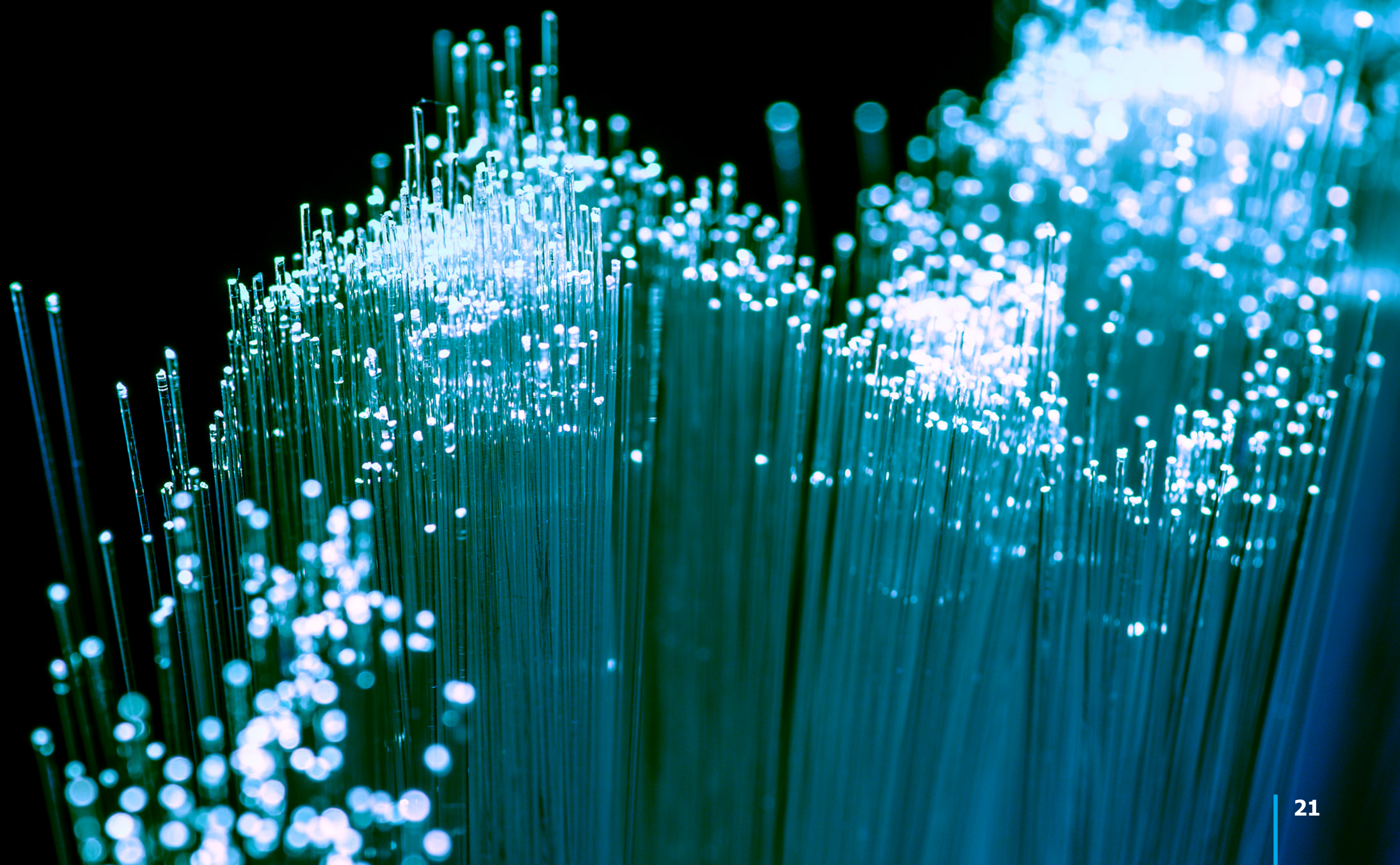
Note: Valid objections to the Commission's decision to proceed under an expedited rule change process close 11 June 2020.

Stakeholder submissions

- Emphasis on providing evidence of impact of COVID-19 on cash flows and feedback on design of proposed deferral mechanism.
- Submissions can be treated as confidential.
- Expedited rule change timeframe means that the AEMC may have limited time to consider later submissions.



STAKEHOLDER QUESTIONS



Next Steps

- Submissions close **25 June 2020**

- To set up a meeting with the AEMC contact:
  - Mitch Shannon: mitchell.shannon@aemc.gov.au
  - Ben Davis: ben.davis@aemc.gov.au

Office address
Level 15, 60 Castlereagh Street
Sydney NSW 2000

ABN: 49 236 270 144

T (02) 8296 7800
F (02) 8296 7899