



11 November 2022

Australian Energy Market Commission
GPO Box 2603
SYDNEY NSW 2000

Lodged electronically: aemc@aemc.gov.au

Reference: RPR0016

Dear Sir/Madam,

RE: Submission to AEMC Review into the arrangements for failed retailers' electricity and gas contracts, Consultation paper

Origin Energy (Origin) appreciates the opportunity to provide a response to the Australian Energy Market Commission's (AEMC) Review into the arrangements for failed retailers' electricity and gas contracts.

The most critical element of a retailer of last resort (RoLR) regime is to ensure that the designated RoLR can recover their costs from the event with certainty and in a timely manner. These conditions are vital to allow the RoLR to manage their risk and avoid contagion.

To the extent that a failed retailer has contracts or hedges that are of value, we consider that any benefit should be realised and used to offset against the costs of the event. This can be achieved through the RoLR cost recovery mechanism framework or allowing the designated RoLR with the right but not the obligation to acquire these contracts. However, the practical application of novating contracts in such circumstances is likely to be complex as we expect there would be a crossover with associated legislation such as insolvency and bankruptcy obligations.

We agree that recent incidents of retailers rapidly increasing prices and encouraging customers to move to alternative retailers while subsequently selling associated contracts at significant profit reflects poorly on the industry and adversely impacts customers. Origin supports a review of this behaviour but considers this is a conduct issue as opposed to a RoLR issue and should therefore be addressed outside the RoLR framework.

It is also important that any proposal to amend the RoLR framework does not create an unnecessary barrier to entry or inadvertently inhibit a retailer from exiting the market under legitimate circumstances. Conversely, the framework should also ensure that retailers are discouraged from using the RoLR process to exit the market for commercial gain.

Origin's response to specific issues identified in the paper are set out below.

Gas RoLR Directions

The Weston Energy RoLR highlights the complexity of intervening in physical gas contracts, especially where multiple retailers are involved. While physical supply was ensured, the relatively high market value of the contracts and the involvement of multiple retailers with differing requirements and arrangements made the novation of contracts largely unworkable. We do not expect the proposed amendments to the RoLR directions framework will resolve these issues.

Notwithstanding, there may be less complex instances where the application of directions to contracts is useful. Origin generally supports amendments to the framework to clarify the circumstances under which a

gas RoLR direction is issued, including allowing the AER to consider the prevailing market conditions and pricing. Applying a materiality threshold would also ensure that directions are issued under appropriate circumstances (e.g. for material RoLR events). Further, Origin considers that the directions framework should be extended to cover all contracts including storage.

We consider that the inclusion of negotiation principles may also be worthwhile, including a requirement that negotiations be conducted in good faith. We would expect that ongoing monitoring and compliance of these principles would be necessary. To the extent that principles are introduced, we consider the existing three-month negotiation period should be maintained. Extending this timeframe delays the cost recovery process.

More generally, we consider that the directions framework should clarify that the designated RoLR is provided the right to take up the failed retailer contracts but is not obliged to do so. Further, it should be clarified that any novation of contracts should ensure that customer benefits are preserved rather than absorbed by the designated RoLR.

Prior to its failure, the AER had no measure of Weston Energy's exposure to spot prices and therefore limited view of its risk of failure. We encourage the AEMC to review existing information and monitoring arrangements to determine if early engagement is possible. Lack of sufficient lead time increases costs and risks to the designated retailer and contributes to a poor customer experience.

Option 1: Cost recovery clarity

A RoLR event can involve substantial costs for the designated retailer and impact the financial stability and market standing for even very large retailers. It is vitally important that the designated retailer is fully compensated for the costs incurred in performing the RoLR function.

While implied in the National Energy Retail Law (NERL), the AEMC proposes to make explicit that RoLR cost recovery includes the wholesale and/or hedging costs incurred to serve the new customers in a defined period after the RoLR event.

Origin supports clarifying the RoLR recovery process to include wholesale and/or hedging costs. Moreover, we consider that the cost recovery provisions should be more explicit to ensure that all legitimate costs incurred by the designated RoLR are provided for, including for example working capital and a competitive margin on costs. In the interest of equity and risk minimisation, it is imperative that the designated retailer suffers no financial penalty as a result of taking on the failed retailer's customers.

Clarifying full cost recovery will also assist the designated RoLR to secure finance should this be required in the period between the RoLR event and eventual payment. In addition, greater clarity on costs may also incentivise smaller retailers to register with the AER to participate as a RoLR. This is an important element to assist the RoLR scheme function effectively and could diversify and reduce the overall risks for each individual retailer. A clear process and right for cost recovery is a key element to making the framework commercially viable and minimising regulatory intervention.

RoLR events are likely to occur in a time of volatile market circumstances and in a compressed timeframe. The compressed timeframes require that the framework is simple and transparent to ensure that customers are appropriately managed to receive continual supply of energy. Effectively managing these elements will reduce customer dissatisfaction and minimise the costs incurred by industry in managing such an event. Any delay in providing cost recovery to the designated RoLR can ultimately increase the designated RoLR's costs and amplify the retailer's risk. This ultimately results in increased costs for customers. It is important therefore that reimbursement occur as quickly as possible. We consider the AEMC should examine the scope for incorporating a timeframe for cost recovery or potential payment program options such as partial payments or full payment based on estimated costs with a subsequent true-up once costs are determined.

Option 2: Matchmaking service

The AEMC proposes that AER information gathering powers be augmented to require failing retailers to provide the AER with information on all contracts held and the associated conditions, including counterparty details. This information would then be shared with the designated RoLR.

Origin supports the provision of additional information that may assist the designated retailer in understanding the failed retailer's contracts and fulfilling its RoLR obligations. In the interest of preserving confidentiality, we would expect that any such information would exclude pricing details associated with the contracts.

To the extent the AER does not have the power to gather the required information, we support the extension of automatic information gathering power to include all contracts held that service its customer load and the conditions under which they are held, including counterparty details. While the information may not eventuate in tangible benefits for the designated RoLR or customers, there may be situations where the information is useful (e.g. reducing search costs etc). We request that any associated information requirements be cross-referenced against existing information gathering powers and information currently collected by other regulatory agencies to ensure minimal duplication.

Options 3a and 3b: Introduce a directions framework with reference to current contract

Under options 3a and 3b, the AEMC proposes a process for novating contracts from the failed retailer to the designated RoLR under a range of contract scenarios. This would require legislative changes that extend to parties outside the energy regulation regime and into contract markets more broadly. Aside from the practical difficulties of implementing legislation that cuts across existing insolvency and bankruptcy legislation, any proposal is likely to increase risk in the contract market as a whole and potentially result in an increased contract risk premium.

We consider the options would be complex and difficult to implement whilst also introducing unintended consequences for the broader contract market. On this basis, we consider there is little benefit in pursuing the options further.

Option 4: Failed retailer funding the cost recovery payments

The AEMC proposes that the RoLR cost recovery scheme include proceeds received through the sale of the failed retailer's 'in the money' hedges, reducing the overall costs to customers.

We note that any attempt to recoup costs needs to ensure that recovery extends to the parent or holding company of the failed retailer to ensure that participants are not incentivised to adopt company structures to avoid the RoLR cost recovery process.

Origin supports measures to recoup costs from failed retailers as a means of funding the designated retailer's RoLR costs, but notes there are likely to be significant operational issues. Prioritising the failed retailer's 'in the money' contracts to offset designated retailers' costs may circumvent some of the contractual issues identified in options 3a and b, however accessing funds prior to other creditors will be complex to implement. Further, RoLR events triggered by an insolvency will also require complex legislative changes that extend into areas outside the energy regulation framework. It is expected that implementing the proposal will add costs to the contract market and increase contract risk.

It is also important to be cognisant of unintended consequences such as encouraging the failed retailer to sell 'in the money' contracts prior to the AER's involvement or disincentivising new retailer market entry due to potential increased cost or risk associated with entry.

We encourage the AEMC to examine potential cost recovery options, including for example allowing the designated RoLR to recover full RoLR costs in a timely manner while the AER pursues 'in the money' contracts. Any recovered funds could be returned to customers once received via distribution charges. This

would reduce costs and risks to the designated RoLR in the period between the event and eventual cost recovery should this occur.

While there are obvious legal and implementation issues associated with the proposal, we consider the option worthy of further examination to determine its viability.

Retailer behaviour

The AEMC recently observed a retailer implementing large and sudden shifts in offers, combined with assertive requests to customers to change retailers, subsequently selling its remaining hedge contracts for substantial profit. The AEMC questions whether further examination of the issue is required.

Origin agrees that such behaviour is undesirable and does not reflect well on the retail industry more broadly. Further, we agree that such behaviour is not in the long-term interest of customers and should be discouraged. We note however that in this instance, the behaviour was not related to a RoLR event but a commercial decision in a volatile market. While further review is warranted, we consider this a conduct issue and as such should be addressed via a separate review focussing on retailer behaviour and consumer impacts. Conduct may be addressed for example through a review of retail licence conditions or of licence compliance monitoring. Any such review requires recognition of potential impacts on incentives for new retailers to enter the market or barriers that may be created for the legitimate exit of retailers from the market.

If you have any questions regarding this submission, please contact Gary Davies in the first instance at gary.davies@originenergy.com.au.

Yours sincerely



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