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Australian Energy Market Commission
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NEM financial resilience – Second Interim Report

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Australian Energy Market Commission (AEMC) on the NEM financial resilience – Second Interim Report.

The esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of 34 electricity and downstream natural gas businesses. These businesses own and operate some \$120 billion in assets, employ more than 51,000 people and contribute \$16.5 billion directly to the nation's Gross Domestic Product.

The esaa welcomes the majority of the AEMC's recommendations; in particular the conclusion that there is no need to apply the G20 measures to the electricity sector. In addition, the following recommendations will limit the risk that a Retailer of Last Resort (RoLR) event will lead to financial contagion:

- the clarification of market suspension rules;
- clarification of retailer of last resort (ROLR) cost recovery arrangements;
- allowing the Australian Energy Regulator to delay designation of a RoLR, and;
- separating out large customers from the RoLR arrangements.

That said, the report overplays the residual risk that remains despite the substantial steps taken by businesses to manage their individual exposures. The esaa acknowledges that there will always be a degree of risk in any market and it is not costless to remove risk. A riskless market is nearly always going to produce sub-optimal outcomes, as the costs of preventing the marginal risk outweigh any potential benefits. In this context, we consider that the following proposals are not proportionate to the notional risk avoided:

- the systemically important market participant;
- the creation of a NEM Resilience Council, and;
- the Special Administration arrangements.

Response to a large participant failure

As part of the approach to dealing with a large participant failure, the AEMC has proposed the creation of a new participant class; systemically important market participant (SIMP). The esaa has concerns the creation of a new class of market participant may lead to differential treatment. All businesses, regardless of their size should succeed or failure on their merit. Some of the discussion in the paper seems to indicate the rules may be applied differently to SIMPs, in the event they experience financial distress. Any variance in the treatment of market participants is likely to have an adverse impact on the market.

NEM Resilience Council

It is important all bodies that have a role in dealing with a retailer collapse communicate, where appropriate, with each other. We expect this would already happen and cannot see the benefit of creating a new standing body, as opposed to the relevant organisations establishing protocols, to enable them to communicate effectively and swiftly with each other in the event of a retailer collapse. The latter is sensible and does not require a new body to be created.

The energy industry is already overseen by numerous agencies and government departments, many of which have sought to increase their remit, resulting in duplicative policy advice and intervention. Another new body would be at inevitable risk of scope creep, which would further muddy the waters. Businesses prior to a collapse, and administrators afterwards, are best placed to make judgements about the position of a company. If, despite these commercial settings, a body is established to assist with a large retailer collapse, its governance must be very tightly controlled. It must have very clear and limited terms of reference relating specifically to its role in relation to a RoLR event, with no scope to increase its remit further. Additionally, membership should be limited to those organisations that already need to make decisions in the event of collapse.

Stability arrangements

esaa continues to support the use of standard administration practices to deal with a failing retail business, regardless of its size. We do not agree with the AEMC's view that administrators will not act in a way consistent with securing supply for customers. While the AEMC specifies that the special administrator would focus on continuity of supply, in all but a narrow set of cases securing supply and getting the best deal for creditors would appear to be closely aligned.

The customer base is the major asset of a retailer. An administrator would attempt to sell the assets to recover money for the creditors, hence maintain supply. While the majority of the customer contracts should be able to be sold, there could be a minority that are not attractive. However, the special administration arrangements also envisage having unsold contracts.

esaa believes special administration is not a proportionate response to the perceived risk of a large retailer collapse, as it would impose certain material costs and inefficiencies now, out of line with the uncertain future benefits. A low likelihood that the amended RoLR creates a risk of contagion in the event a large retailer fails does

not justify fundamental changes to Australia's insolvency laws altering the rights and responsibilities of lenders, owners, directors and administrators. Further, the proposal is not well targeted as it will have an impact on many aspects of energy sector beyond the root causes of any potential cascading retailer failure.

Any questions about our submission should be addressed to Fergus Pope, by email to fergus.pope@esaa.com.au or by telephone on (03) 9205 3107.

Yours sincerely



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