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A few words.

25 September 2014

John Pierce
Australian Electricity Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Dear Mr Pierce

NEM Financial Market Resilience –Second Interim Report

AGL Energy Ltd (AGL) welcomes the opportunity to respond to the AEMC's Second Interim Report *on NEM Financial Market Resilience* (the Paper).

AGL has been actively engaged in the AEMC's review of financial resilience in the National Electricity Market (NEM), which the Paper is a part of. As one of Australia's largest vertically integrated retailers of electricity with more than two million customers and over 10,500 MW of generation capacity in the NEM, AGL appreciates the practical implications that any proposed financial market reforms will have on the market. The following are our views on the proposals raised in the Paper.

Electricity financial market reform
AGL welcomes the AEMC's recommendation that none of the G20 OTC reforms or any other additional regulatory measures be implemented in the electricity financial market. It agrees with the AEMC that a case has not necessarily been made for additional measures, given the low risk of contagion, the costs and regulatory burden of additionalmeasures and furthermore, that many measures attempting to regulate the OTC electricity market may actually be counterproductive.

Changes to the Retailer of Last Report (ROLR) scheme
AGL is supportive of most of the recommendations proposed by the AEMC regarding the ROLR scheme as a way of reducing the risk of contagion. Most are well targeted at reducing the immediate cash flow impacts on the ROLR, thus minimising the risk of further retailer failure. However, some recommendations need to be balanced with the cost and impact they may have on the market.

Recommendation 1: Revised Cost Recovery Arrangements

While the proposed changes to the cost recovery arrangements will not reduce the immediate cash flow obligations on the ROLR, AGL is supportive of the changes as they will provide greater clarity and certainty to the ROLR regarding cost recovery. However, there would be merit in considering whether the AER can provide the ROLR with recovery of costs in a shorter timeframe in order to minimise the risk of financial contagion in the short term.

Recommendation 2: Delayed Designation of ROLRs

AGL is supportive of a short delay in the designation of the ROLR(s), if it assists the AER in the allocation of customers. However, the AER should continue to maintain a market driven allocation through voluntary pre-registration of interest as it currently exists.

Recommendation 3: Exclusion of Large Customers from ROLR scheme

AGL considers there is some merit in excluding large customers from the ROLR scheme, based on the following conditions. The first condition being that the large customer is not required to enter into an agreement with an alternative ROLR prior to its existing retailer defaulting. This is because it is costly and impractical to expect customers, even large ones, to negotiate a separate agreement with another retailer when there is a low probability of their current retailer failing. Secondly, the consumption threshold for exclusion from the ROLR scheme should be increased from 10GWh/year to 30GWh/year. This is because customers with significant levels of consumption are more likely to be sophisticated customers and therefore more capable of dealing with the administrative issues associated with being excluded from the ROLR regime.

In addition, it needs to be considered whether customers whose business operations are important to the economy should be faced with disconnection in the event that they are unable to procure another retailer within 7 days of their retailer defaulting. There are also other practical issues that need to be considered, such as in the event that a customer is unable to procure an alternate retailer within the 7 day timeframe, who is responsible for its usage while it was connected and who pays for its disconnection.

Recommendation 4 and 5: Delaying Credit Support Requirements of AEMO and DNSPs

AGL is supportive of the recommendations to delay the credit support requirements of the ROLR by one week for AEMO and the DNSP respectively. This will provide the ROLR more time to procure credit support and minimise the upfront financial obligations on the ROLR.

Recommendation 6: Improvement of Customer Information and Systems

AGL is supportive of the recommendation to improve access to customer information and systems to enable the smoother and quicker transition of customers to the ROLR. However, any such improvements should not incur material costs and administrative burden on market participants.

Market Suspension of Generators
AGL considers that there is merit in the AEMC's proposal to allow the possibility of a generator to continue operating even though it may be in external administration. As noted by the AEMC, the continued operation by the generator may be necessary for system security and may also ease the financial distress of the entity. However, factors that need to be considered in further developing this proposal include: the duration of operation while under administration, the materiality of the generator for NEM security of supply, and whether there is sufficient personnel and resources to continue operation.

Separate Framework for Systemically Important Market Participants (SIMPs)
The AEMC's proposal to implement a separate framework for dealing with SIMPs in distress, seems appealing in theory, but has some practical issues that need to be addressed. Firstly, setting up a structured decision making framework and involving several government bodies in the decision making process such as the NEM Resilience Council, may compromise the swift and flexible response that is required when dealing with a financially distressed market participant. While we consider that there is a role for government in the event that a SIMP fails, and that role should be clarified, we are concerned that setting up an additional body may add to the regulatory burden on industry. However, if several bodies were included in the decision making process, it would be prudent to involve industry in the process as well. This is because market participants would be the best at determining how issues such as a large transfer of customers and significant requirement for credit support would impact them. In addition, the development of any broad decisions regarding the behaviour and future of the market participant needs to consider how it fits in with the commercial decision making powers of the external administrator.

Stability Arrangements
AGL is concerned with the alternatives to the ROLR scheme that are being proposed. The case has not been made for measures such as an special administrative regime as they are complex and there is no evidence that the modified ROLR and traditional insolvency measures are insufficient in reducing the risk of contagion. These measures known as stability arrangements involve significant changes to legislation and funding provisions that extend well beyond the electricity regulatory framework. Any changes of this magnitude must be exercised with caution given the significant implications they will have on the physical and financial electricity markets. Given these issues, AGL does not consider there is justification for developing separate stability arrangements and a special administrative regime to deal with a financially distressed market participant.

In summary, AGL supports many of the proposed modifications to the ROLR scheme, as a way of reducing the risk of contagion. However, it is wary of broader changes aimed at reducing the risk of contagion in the NEM. It considers that any significant changes to the decision making framework in response to a financially distressed market participant and alternatives to ROLR such as stability arrangements and special administrative regimes should be exercised with caution given their complexity and impacts they will likely have on the market.

If you have any queries about the submission or require further information, please contact Josynta Singh at jsingh@agl.com.au or on 03 8633 6628.

Yours sincerely,

Simon Camroux
Manager Wholesale Markets Regulation
AGL Energy Ltd