



20 July 2012

Mr John Pierce
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Submitted by: www.aemc.gov.au

Dear Mr Pierce

EMO0024 - NEM FINANCIAL MARKET RESILIENCE - ISSUES PAPER

Origin Energy (Origin) appreciates the opportunity to provide the Australian Energy Markets Commission (AEMC) with comments in relation to its Issues Paper on NEM financial market resilience.

Financial arrangements and markets across the NEM are generally robust

Origin agrees with the AEMC that the financial relationships and markets underpinning the efficient operation of the National Electricity Market (NEM) are generally robust. The success and viability of an electricity business is dependent upon its ability to manage risk efficiently and effectively. Managing market, credit and operational risk are the core business functions of electricity market participants. They therefore have a strong incentive to develop and enforce risk management policies and procedures that promote prudent financial arrangements.

As such, the financial arrangements underwriting hedge and derivative contracts are subject to rigorous risk management frameworks, prudential and margin requirements in addition to other financial requirements associated with holding an Australian Financial Services Licence (AFSL). These are all subject to audit and periodic or ad hoc reviews ensuring ongoing suitability.

Generators, retailers or financial intermediaries enter into exchange traded or tailored over-the-counter (OTC) derivative or hedge contracts with counterparties that are subject to risk assessment or predetermined prudential and margin requirements. The Australian Energy Market Operator (AEMO) and Australian Stock Exchange (ASX) both have strict prudential and margin requirements to ensure the systemic viability of the respective markets in the event of default. OTC counterparties are subject to rigorous risk assessment where additional parent company or bank guarantees may be sought to provide the issuer additional financial security.

In addition to external statutory risk controls, prudent physical market participants and financial intermediaries have clearly defined internal risk management frameworks. These frameworks are mandated and auditable under AFSL conditions. These risk frameworks are generally Board endorsed policies and procedures that establish risk limits with management and operational committees. These committees and responsible officers ensure compliance with the policies and procedures and operate the business within the designated risk limits.

NEM participants operate in a risk management conscious environment that is designed to promote prudent decision-making in a way that helps manage the risk of financial contagion.

Testing the Retailer of Last Resort (RoLR) arrangements

Origin notes that financial contagion risks in the NEM could arise if the RoLR arrangements were unable to manage the failure of a large retailer. The financial contagion risk sits with the default RoLR and its ability to manage the risks imposed upon it following a RoLR event. The market managed the only two RoLR events to date relatively smoothly. The customers of Energy One in 2007 and Jackgreen in 2009 were rolled into the customer base of incumbent retailers without incident. Both were small retailers with limited liabilities imposed on the acting RoLR.

The risks associated with the default of a large retailer are exponentially larger, however, with potentially systemic implications. Compared to the RoLR events to date, the default RoLR may find it more challenging to access in a timely manner sufficient prudential and contract coverage to manage its increased load. This could result in financial stress, and, at an extreme, could trigger a second default event. We consider the AEMC's paper captures these risks accurately, and the cascading scenario under which they may occur.

We therefore support the AEMC reviewing the existing RoLR framework to ensure it does not pose a potential risk to the stability of the NEM.

Further discussions

Should you have any questions or wish to discuss this information further, please contact Hannah Heath (Manager, Regulatory Policy) on (02) 9503 5500 or hannah.heath@originenergy.com.au.

Yours sincerely,



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