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25/06/2020

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

Lodged online via: www.aemc.gov.au

Dear John,

Submission to the AEMC's deferral of network charges rule change consultation paper

TransGrid is the operator and manager of the high voltage transmission network connecting electricity generators, distributors and major end users in New South Wales and the Australian Capital Territory. TransGrid's network is also interconnected to Queensland and Victoria, and is instrumental to an electricity system that allows for interstate energy trading.

TransGrid acknowledges the significant impact on the Australian economy, including energy customers, of the COVID-19 health crisis. Networks are providing voluntary support to retailers to help alleviate the impact of this health crisis on customers. TransGrid will continue to do its part to support end use customers throughout this time.

The Australian Energy Regulator (**AER**) has requested the AEMC to change the National Electricity Rules (**NER**) to defer the payment by retailers of network charges incurred between 1 July 2020 and 31 December 2020 for up to six months. The deferred charges would relate to small customers whose capacity to pay has been affected by COVID-19.

TransGrid considers that the AEMC should not make a rule because no material issue has been identified. The AER has not shown that the impacts of COVID-19 on retailer cash-flows are significant and cannot be managed, or that any flow on implications for the effectiveness of retail competition are material. Furthermore, the proposed changes would have very significant cash-flow and financeability impacts on network businesses that would ultimately increase costs for consumers while resulting in no identifiable benefits.

TransGrid is currently investing in a number of large transmission projects to support the secure and reliable operation of the NEM and cash-flow management is a critical issue for the business. As a net investor in the economy, TransGrid will be particularly impacted by the proposed changes.

In the event that the AEMC finds evidence that there is a material issue to address and considers that making the rule will result in net benefits to consumers, any rule made should:

- **be targeted at retailers in genuine financial distress as a result of the COVID19 pandemic** due to payment difficulties being faced by their customers.
- **allow for flexible and fit-for-purpose implementation of the deferral arrangements** between the relevant businesses in order to avoid the costs and risks that may result from complex and prescriptive arrangements being set out in the rules.
- **apply consistently across the National Electricity Market (NEM)**. If in practice any rule made to defer payment of network charges is likely only to apply in some NEM jurisdictions

it will not achieve its intended purpose (and should not be made), given many retailers have customers across the NEM regions.

TransGrid's detailed comments on the AER's rule change proposal are provided in the **attached** submission.

We appreciate the opportunity to make this submission. Given the potentially significant impact of the proposed rule on network businesses, we encourage the AEMC to extend the time for making its draft rule to provide further opportunity for stakeholder consultation, including a short consultation on any draft rule proposed to be made by the AEMC. If you would like to discuss this submission, please do not hesitate to contact me or Catriona Webster, Head of Public Policy, on 0447 124 726.

Yours faithfully

Eva Hanly
Executive Manager, Strategy, Innovation & Technology

Deferral of network charges

TransGrid submission to the AEMC's consultation paper

TransGrid

1. Overview

The Australian Energy Regulator (**AER**) has requested the AEMC to change the National Electricity Rules (**NER**) to defer the payment by retailers of network charges incurred between 1 July 2020 and 31 December 2020 for up to six months. The deferred charges would relate to small customers whose capacity to pay has been affected by COVID-19.

1.1 Synopsis of submission

The proposed changes would have very significant cash-flow and financeability impacts on network businesses that would ultimately increase costs for consumers while resulting in no identifiable benefits. In particular, there is no evidence:

> that the impact of COVID-19 on retailers' cash-flows is significant
> that any impacts cannot be effectively managed by a range of tools available to retailers (e.g. by accessing debt or equity capital markets, changing retail prices or reducing short-term discretionary costs)
> that deferring a small portion of network charges will restore the financial viability of any retailers experiencing cash-flow pressures, or
> that any retailer failures could lead to:
  – adverse impacts on the effectiveness of retail competition, or
  – greater systemic consequences due to any inadequacy of the prudential arrangements that support NEM settlements and the retailer of last resort (**RoLR**) arrangements that manage the process of retailer failure

TransGrid therefore considers that the AEMC should not make a rule. Evidence of a material issue that needs to be addressed has not been provided and the proposed rule will have unintended consequences on on the working capital positions of network businesses which have already been impacted by COVID-19. If the rule is made as proposed, the working capital positions of Networks will be further impacted, leading to increased costs for electricity consumers, which is not in their long term interests.

In the event that the AEMC finds evidence that there is a material issue to address and considers that making the rule will result in net benefits to consumers, any rule made should:

> **be targeted at retailers in genuine financial distress** as a result of the COVID19 pandemic due to payment difficulties being faced by their customers
> **allow for flexible and fit-for-purpose implementation** of the deferral arrangements between the relevant businesses in order to avoid the costs and risks that may result from complex and prescriptive arrangements being set out in the rules, and
> **apply consistently across the National Electricity Market** (**NEM**). If in practice any rule made to defer payment of network charges is likely only to apply in some NEM jurisdictions it will not achieve its intended purpose (and should not be made), given many retailers have customers across the NEM regions.

1.2 Targeting the rule change to retailers in genuine financial distress

The AER's proposal is that all retailers can access deferred network charge payment arrangements and get cash-flow support from network businesses. If a rule of this broad scope was made it would result in very significant consequences for networks' cash-flow and financeability and ultimately result in increased costs to consumers. However, if the rule made is targeted to retailers in genuine financial distress as a result of the COVID19 pandemic due, these adverse impacts on consumers would be reduced. In order to appropriately target any rule made, we propose that:

> **The three largest retailers and Government-owned retailers should be excluded from the operation of the rule** on the basis that there is no evidence that these retailers are in financial distress or require cash-flow support from networks.
> **Other retailers should be required to demonstrate eligibility for cash-flow support** under arrangements similar to those implemented by the New Zealand Electricity Authority. To be eligible for support under the rule, retailers should be required to demonstrate, and have an accountant certify, that, as a result of COVID 19, they have experienced material cash-flow impacts which will place their solvency at risk in the absence of the relief being provided under the rule.
> **The scope of the consumers in relation to whom retailers are able to defer network charges should only include small customers genuinely impacted by the economic fallout from the COVID-19 health crisis.** Large and industrial customers should be excluded from eligibility. For such large customers individual contracts and arrangements should address the risk of customer default.

1.3 Flexible, fit-for-purpose implementation of the deferral arrangements

Under the proposed rule, retailers would be able to defer payment of certain network charges to distribution networks for 6 months. The deferred amounts would include both the distribution component of those network charges and the transmission component (collected by the distributor on behalf of the relevant transmission business).

TransGrid recognises that if retailers defer payment of network charges to TransGrid's distribution customers, but those businesses are still required to pay TransGrid on time, this would worsen the impact of the rule change on its distribution customers' cash-flows and financeability. For this reason, TransGrid accepts that, as proposed by the AER, its distribution customers should be able to withhold a reasonable amount from transmission networks to account for the fact that retailers will be deferring payment of transmission charges as well as distribution charges.

However, **TransGrid considers that a prescriptive approach in the rules implementing the deferred payment of transmission charges by distribution businesses would present high risks of unintended consequences**. Accordingly, we propose a flexible approach that:

> sets the principle in the rules that transmission businesses should bear a share of any deferred payment by retailers of network charges equivalent to the transmission component of the charges, and
> requires transmission and distribution businesses to negotiate in good faith and agree the recovery arrangements between them to reflect the principle in the rules.

This approach would allow for equivalent arrangements to those underpinning the network business' voluntary tariff relief package to be agreed between the parties, which differ across jurisdictions.

It is not appropriate to expose transmission businesses to risks of retailers ultimately defaulting on their payments to distribution businesses. There are clear and appropriate mechanisms under the rules for distribution businesses to manage those risks and costs including a specific retailer insolvency event cost pass through, and no avenues for transmission businesses to do so (either under the national energy laws or under the general legal frameworks that apply to the administration of insolvent corporations). Exposing transmission businesses to such risks would be inconsistent with the regulatory framework for managing retailer default established under the national energy laws and would only manifest in additional costs (e.g. financing costs), which would ultimately be borne by consumers.

1.4 Structure of this submission

TransGrid's response to the issues raised in the AEMC's consultation paper is set out in the sections below. The sections relate to:

> the need for the proposed changes
> the scope of the changes, including:
  – eligibility of retailers

  - coverage of end-use customers, and
  - deferral period
- the application to transmission, and
- the costs and benefits.

2. Need for the proposed changes

TransGrid considers there is no identified material issue that needs to be addressed in the manner proposed by the AER. The AER has not shown:

- that the impact of COVID-19 on a material set of retailers' cash-flows is significant
- that any impacts cannot be effectively managed by a range of tools available to retailers
- that deferring a small portion of network charges will restore the financial viability of any retailers experiencing cash-flow pressures, or
- that any retailer failures could lead to:
  - adverse impacts on the effectiveness of retail competition, or
  - greater systemic consequences due to any inadequacy of the prudential arrangements that support NEM settlements and the retailer of last resort (RoLR) arrangements that manage the process of retailer failure

If any of these matters is not satisfactorily proven, the AEMC should not make the changes as proposed.

2.1 Impact of COVID-19 on retailer cash-flows

While it is clear that the COVID-19 health crisis has caused increased levels of hardship for some small customers, there is limited evidence of significant adverse impacts on retailer cash-flows.

The AER considers that cash-flows of some retailers are likely to be under pressure due to increasing bad debts and reduced revenue from consumption, while fixed costs remain stable (such as network bills and wholesale bills after hedging is taken into account). However, cash-flow implications for retailers are likely to be tempered by a range of factors:

- While the AER notes in its rule change proposal that 20,000 customers have registered for payment plans since early March 2020 and over a thousand customers per week are seeking assistance from retailers, it has not demonstrated that this is a material increase from business as usual. Conversely, the AER's COVID-19 Retail Market Data Dashboard shows that since March 2020 there does not appear to have been a material increase in the proportion of customers on or entering into payment plans or hardship arrangements.[1]
- While overall electricity consumption in the NEM is around 5% lower than at the same time last year, the reduction is not material and is partly accounted for by milder weather conditions.[2] The reductions in demand are certainly less significant than reductions in overseas jurisdictions that experienced more restrictive measures to halt the spread of COVID-19 (such as the closure of heavy industry).
- Any reduced revenues due to increased bad debts or reduced consumption may in part be mitigated by lower wholesale costs. While we acknowledge that some retailers will not gain the full benefit of reductions in wholesale market prices because of their hedging arrangements, it should be noted:
  - vertically integrated retailers are likely to receive the net benefits of lower wholesale costs (regardless of whether the benefit accrues on the retail or generation side), and
  - smaller and mid-sized retailers may receive some benefits from vertical integration, but are also likely to have some flexibility built into their hedging strategies enabling them to take advantage of lower wholesale costs at least by 1 July 2020, when the AER proposes the rule should commence.

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[1] See: https://www.aer.gov.au/retail-markets/performance-reporting/retail-market-data-dashboard-covid-19.

[2] See AGL presentation to Macquarie Australia Conference, May 2020: https://www.asx.com.au/asxpdf/20200505/pdf/44hkk5zp3cr3mb.pdf.

> While some costs faced by retailers are fixed, risks associated with changes in consumer demand should be managed in the tariff structures offered to consumers (e.g. by covering such costs in the fixed component of the tariff). Any cash-flow impacts from reduced consumer demand should therefore be mitigated by appropriate risk management practices by retailers.

In the absence of transparent "open book" evidence of severe impacts on retailer cash-flows, it is not open to the AEMC to conclude there is a material issue to be addressed. The available evidence in the market does not show any trends toward significant cash-flow impacts. As there is no clear evidence of a material issue that should be addressed, a rule should not be made.

2.2 Retailer management of cash-flow risks resulting from COVID-19

Retailers are generally able to utilise a rage of tools to manage their cash-flows, most of which can be implemented rapidly in response to emerging cash-flow issues. The AER has not shown that, even if retailers were to experience material impacts on cash-flows due to COVID-19, they do not have the tools available to manage those impacts.

Retailers may be in a position to manage any impacts on cash-flows through one or more of the following:

> Changing financial arrangements with lenders, such as extending credit arrangements. It is appropriate that financial institutions (not network businesses) extend credit to retailers, which they should do on competitive terms. In this regard it should be noted that Australian banks, supported by the Reserve bank, regulatory agencies and the Government, have put in place a substantial program of credit support precisely so businesses are positioned to meet their debts as and when they fall due.

> Obtaining further operating capital from existing or new equity providers. This is of course most achievable for government owned entities, but also viable and achievable in tight timeframes for both publicly and privately held corporations, as can be seen from recent equity raising by consumer focusing firms such as Flight Centre[3] and Breville Group,[4] and has been supported by temporary policy waivers by ASIC and the ASX.[5] There is no clear reason why consumers should pay higher costs associated with transferring cash-flow risk upstream to networks, rather than allowing equity holders to work out an appropriate solution, supported by current COVID-19 policies.

> Changing retail prices to account for additional risks and costs being managed. Retailers change their prices in most NEM jurisdictions on or around 1 July each year, which would appear to give them a timely opportunity to use this tool to manage their cash-flows.

> Reducing short-term discretionary operating costs (such as customer acquisition costs) until cash-flow pressures ease.

> Selling assets (including customer contracts). It is highly unlikely that the level of bad debts held by small customers would increase so rapidly and significantly that there would be no market for the voluntary sale of their customer base.

The AEMC should critically evaluate whether the proposed arrangements to defer payment of some network charges are appropriate and proportionate. This evaluation should carefully weigh:

> whether there are any residual cash-flow issues for specific retailers (after the retailer has exhausted all the tools available to it to manage the issue), and

> whether the scale of any deferred payments under the proposed arrangements are able to effectively address those residual cash-flow issues.

If there are no material residual cash-flow issues, or if the proposed changes do not effectively address the nature of any cash-flow issues that do arise, the changes should not be made as proposed. If the proposed changes do not address any material cash-flow issues arising, it is then likely that the issue is not created by network charges. If this is the case, the AEMC should look to the relevant cause of the cash-flow issues to address them (e.g. by allowing deferred payment of wholesale market settlements).

[3] https://www.fctgl.com/wp-content/uploads/2020/04/2051198.pdf

[4] https://brevillegroup.com/wp-content/uploads/2020/06/2074909.pdf

[5] https://www.afr.com/wealth/personal-finance/everything-you-need-to-know-about-covid-19-capital-raisings-20200415-p54jwv

2.3 Consequences of retailer failure

It is not clear that any retailer failures would be an unacceptable or problematic outcome, even where there is evidence showing that some retailers are facing cash-flow impacts they are unable to manage. The competitive process has always involved the failure of some service providers. This is part of a process that should, all things being equal, improve outcomes for consumers. Service providers that fail are those unable to provide services that consumers value (including managing risks on their behalf) at an acceptable price. Where there are no underlying issues with market structure, this process should leave behind a set of effective competitors vying to provide a range of differentiated services that consumers value, at competitive prices.

The AER has not shown how any retailer failures likely to result from COVID-19 would subvert the ordinary operation of this competitive process. Evidence supporting this proposition would need to show that there is a material risk that the effectiveness of retail competition is threatened due to:

- loss of retailers providing critical mass to the competitiveness of the retail market (i.e. second and third tier retailers whose existence puts effective price discipline on the retail market)
- loss of retailers providing product differentiation or services valued by specific sub-sets of consumers (e.g. small business consumers or solar consumers).

The AEMC's annual retail competition reviews do not appear to have identified underlying issues with retail market structure in the NEM. The risk of failure of a small number of retailers due to COVID-19, which we consider to be low, is unlikely to threaten effective retail competition in the NEM. Experience has also shown that barriers to entry are low, with new retailers regularly entering the market to provide a range of differentiated electricity retail products and services. Accordingly, any material impacts on the effectiveness of retail competition, as unlikely as that is, would likely be temporary.

The AER has also not shown how any current risks could manifest in greater systemic consequences, including through cascading failures. Doing so would necessitate highlighting specific inadequacies in the prudential arrangements that support NEM settlements and the RoLR arrangements that ensure continuity of essential services for customers in the event of retailer failure. Without specific issues being shown to arise from these arrangements, it has not been established how cascading failures could occur that would necessitate the changes proposed by the AER.

3. Scope of the changes

There will be real costs borne by consumers resulting from the transfer of cash-flow risk from retailers to networks (discussed further in **Section 5** below). It is therefore critical to mitigate those costs by limiting the scope of any new arrangements so they are targeted to address the specific material issues found to be present. In particular, a targeted scope of the arrangements should place clear controls around:

- the eligibility of retailers under the arrangements
- the scope of the customers in relation to whom retailers are able to defer network charges, and
- the duration of the arrangements.

These matters are considered in turn in the sections below.

3.1 Retailer eligibility

Retailers eligible for assistance under any arrangements introduced by the AEMC should be limited to an identified class of retailers that need the assistance, and for whom the assistance would make a tangible difference. Eligible retailers should be those who, despite managing their costs and risks effectively, due to COVID 19:

- are at risk of not being able to pay their debts as and when they fall due, and
- the deferred payment of some network charges would remove that risk.

In our view any retailers potentially at risk of experiencing cash-flow issues are likely to be smaller niche retailers who may cater to a market particularly impacted by the COVID-19 health crisis (e.g. retailers that target small businesses). An appropriate approach to targeting this group of retailers would be to:

> exclude designated RoLRs (i.e. the big three vertically integrated retailers)
> exclude government owned retailers (e.g. Aurora, Red Energy etc.), and
> only include retailers who are able to prove, based on objective metrics, that their cash-flows have been significantly affected by COVID-19 and that deferral of network charges will place them back into a stable financial position.

There is no evidence that designated RoLRs or Government-owned retailers are in financial distress or require cash-flow support from networks. Exclusion of Government-owned retailers would also be consistent with the policy approach of the Australian Government of not extending COVID-19 assistance programs, such as the Job Keeper wage supplement program, to state government agencies including local governments.

This approach would be broadly consistent with the scheme introduced by the New Zealand Electricity Authority. Retailers may access that scheme where an independent accountant (auditor) certifies that:

(a) the retailer's overdue receivables have:
    (i) increased by more than 25% since the same month in 2019, or
    (ii) if the retailer was not trading in the same month of 2019, increased by more than 25% since March 2020, and
(b) in the opinion of the auditor:
    (i) the retailer has, or in the next 6 months immediately following the date of the certificate is likely to have, significant liquidity problems
    (ii) the liquidity problems are, or will be, a result of the effects of COVID-19 on any one or more of the retailer, the retailer's creditors, and the retailer's debtors
    (iii) the retailer satisfies the relevant test for solvency in the Corporations Act 2000, and
    (iv) it is more likely than not that the retailer will be able to pay its due debts within 12 months

Taking a similar approach would provide targeted support to retailers for whom a deferral of network charges would make a material difference to their ongoing solvency. A clear and efficient process to assess retailer eligibility should be designed so that there are not material barriers in place to small retailers efficiently receiving any assistance they genuinely need.

If the AEMC does not consider it appropriate to introduce such an independent process to verify that a retailer requires support, then it would be necessary to introduce another method of ensuring that support is appropriately targeted. An important aspect of this would likely be the charging of interest at a rate that is slightly higher than the rate of interest that commercial lenders ordinarily charge to small or niche electricity retailers for working capital.

3.2 Scope of customers covered

Any arrangements should only relate to small customers genuinely impacted by the economic fallout from the COVID-19 health crisis. The arrangements should therefore relate to small customers who enter into:

> a payment plan or instalment arrangement, or
> any arrangement as a hardship customer.

The arrangements should not apply to customers who enter into the broader category of "deferred debt arrangement" unless this concept is limited to small customers. Large and industrial customers should be excluded from the scope of the arrangements. For large customers individual contracts and arrangements (such as credit support) should specifically address the risk of customer default. Retailers also have more tools available to manage those risks, including the disconnection of that customer (subject to their contractual arrangements).

This approach would limit the arrangements to apply to small customers whose ability to pay their electricity bill has been compromised by the impacts of COVID-19. It is appropriate that the arrangements be limited as proposed above in order to mitigate the impact of unnecessarily transferring additional cash-flow risks and costs to network businesses.

3.3 Duration of arrangements

In order to minimise the cost impacts of any deferred network charge payment arrangements (such as increased risks and financing costs), they should be clearly limited in duration. An application period of no more than six months would be appropriate.

The economic and social impacts of COVID-19 continue to evolve. It is therefore difficult to predict with certainty whether the issues that any deferral arrangements were made to respond to will be present for a more extended duration. If the issues do persist, the appropriate process to consider the extension of the arrangements should be a further rule change process overseen by the AEMC. The AEMC has shown it can quickly consider such issues under an expedited rule change process.

The AEMC will also be well placed to consider whether the arrangements should be extended, given it has managed the initial rule change process. If requested to do so, the AEMC should only extend the application of any deferred debt arrangements where:

- the arrangements have been effective in practice for the initial period of application, and
- any issues that the arrangements were made to respond to (e.g. the rapid deterioration of customer debt levels) are clearly and objectively shown to persist.

4. Application to transmission

Under the proposed rule, retailers would be able to defer payment of certain network charges to distribution networks. The deferred amounts would include both the distribution component of those network charges and the transmission component. The transmission component is collected by the distributor from the retailer on behalf of the relevant transmission business.

This section of the submission sets out TransGrid’s views on:

- potential impact of the proposed changes on TransGrid
- appropriate approach to implementation, and
- appropriate treatment of retailer default risks.

4.1 Impacts of the proposed changes on TransGrid

TransGrid recognises that if retailers defer payment of network charges to TransGrid’s distribution customers but those businesses are still required to pay TransGrid on time, this would worsen the impact of the rule change on its distribution customers’ cash-flows and financeability. Indeed, we understand the potential impacts of the proposed changes are very significant for distribution businesses. For this reason, TransGrid considers its distribution customers should be able to withhold a reasonable amount from transmission networks to account for the fact that retailers will be deferring payment of transmission charges as well as distribution charges. TransGrid has assessed the impacts of the proposed rule change on this basis.

This rule change has been proposed at a time when TransGrid is already under considerable cash-flow and financeability pressures due to:

- requirements for major investment in transmission infrastructure in NSW, and
- costs incurred as a result of events beyond our control.

TransGrid has embarked on a number of large transmission projects to support the secure and reliable operation of the NEM. The projects are complex and large in scale. TransGrid has been required to fund on its current balance sheet:

- approximately $30 million dollars of unavoidable cost increases in the Power Sydney Futures project, and
- tens of millions of dollars of the early works required to deliver large greenfields transmission projects within the time required by Government stakeholders.

TransGrid's financial position has also been impacted by costs associated with events outside its control. In the 2020 financial year TransGrid's cash-flow was significantly impacted by the bushfires. TransGrid incurred approximately $20 million of costs to repair bushfire damage. TransGrid's costs have also increased due to increased statutory charges imposed by the NSW Government on networks, such as Land Tax and Carbon Offset Funds.

In addition, TransGrid's cash-flows have been directly impacted in financial year 2020 as a result of under-recovery of revenue because of COVID-related demand reductions. These under-recoveries will continue to be experienced by TransGrid in the 2021 financial year as transmission prices for that year were set prior to COVID.

This is the environment that forms the starting point for any cash-flow implications for TransGrid that would flow if the proposed changes were to be made. TransGrid's high level modelling of those implications are a peak cumulative cash-flow impact of close to $70 million. If the rule is made as proposed, the working capital position of TransGrid will be further impacted, leading to increased costs for electricity consumers, which is not in their long term interests.

The security and reliability of the transmission system is paramount and expenditure on network operational activities must be prioritised to ensure that security and reliability are maintained. For this reason, if TransGrid is required to provide cash-flow support to retailers it will need to review its investment in large transmission projects and consider reductions in staff.

In considering whether the proposed rule is in the long term interests of electricity consumers, the AEMC must consider the cumulative effect of these impacts on all network businesses and how these will flow on to consumers. Any benefits of the proposed changes must be clear and unambiguous to justify the acceptance of these impacts.

4.2 Approach to implementation

A prescriptive approach in the rules implementing the proposed changes would present risks of unintended outcomes. TransGrid suggests a high level principle should be to favour flexible arrangements that allow parties to find workable solutions to implement the intent of the arrangements.

The process in the rules for allocating transmission charges and billing transmission customers for prescribed transmission services involves considerable complexity. The process is practically managed slightly differently in different NEM regions. In these circumstances the implementation of arrangements for the deferred payment by distribution businesses of transmission charges would present high risks of unintended consequences.

Accordingly, we propose a flexible approach that:

> sets the principle in the rules that transmission businesses should bear a share of any deferred payment by retailers of network charges equivalent to the transmission component of the charges, and
> requires transmission and distribution businesses to negotiate in good faith and agree the recovery arrangements between them to reflect the principle in the rules.

This approach would allow for equivalent arrangements to those underpinning the network business' voluntary tariff relief package to be agreed between the parties, which differ across jurisdictions.

4.3 Treatment of retailer defaults

The AEMC's consultation paper notes that detailed implementation of the changes within the rules could require the inclusion of arrangements for transmission businesses to recover defaulted payments by failed retailers.

TransGrid considers it is not appropriate to expose transmission businesses to risks of retailer default. There are clear and appropriate mechanisms under the rules for distribution businesses to manage those risks and costs including a specific retailer insolvency event cost pass through. There are no avenues for transmission businesses to recover such defaulted amounts. There is no direct contractual relationship between a transmission business and retailers. There is accordingly no ability for a transmission business to:

- manage the risks of retailer default through the application of prudential or credit support arrangements, or
- prove debts that could be recovered under the general legal frameworks that apply to the administration of insolvent corporations.

In these circumstances, it is not appropriate to expose transmission businesses to risks they are unable to manage. Doing so would only manifest in additional costs (e.g. financing costs), which would ultimately be borne by consumers. Moreover, the transfer of retailer default risk from distribution businesses to transmission businesses is not necessary to achieving the desired outcome, which is to provide cash-flow relief for some retailers.

5. Costs and benefits

The AEMC should only introduce measures to address those issues if the benefits of doing so outweigh the costs for consumers. TransGrid's view is that the contrary is true. The costs of introducing the proposed rule (discussed in **Section 5.2** below) clearly outweigh the benefits (discussed in **Section 5.1**). Accordingly, a rule along the lines of that proposed by the AER should not be made by the AEMC.

If deferred network charge payment arrangements are introduced:

- the scope of the arrangements should be clearly targeted to minimise any adverse impacts for consumers, and
- the arrangements should allow parties the flexibility to negotiate and agree relevant details of implementation to minimise any unintended outcomes.

In order to be effective, any arrangements introduced should apply consistently across the NEM. If, in practice, any rule made is likely only to apply in some NEM jurisdictions, it will not achieve its intended purpose (and should not be made). A retailer with customers across NEM jurisdictions is unlikely to obtain sufficient cash-flow relief to remain solvent if it is only able to defer network charges in some regions.

5.1 Benefits

The AER has not identified material benefits for consumers that would result if the proposed changes were introduced. As shown in **Section 2** above, there is no evidence of a clear threat to retailer solvency due to the COVID-19 health crisis, and no consequential threat to the effectiveness of retail competition. The AER's proposed changes are therefore unlikely to materially reduce risks to the effectiveness of retail competition.

The most compelling case for a potential consumer benefit could be from a reduced risk of cascading retailer failure. Such an outcome, were it to occur, could lead to significant bad debt residing with RoLRs, placing their solvency and the system itself under threat. Putting aside the proposition that the proposed changes would be an inadequate intervention to address a clear risk of cascading retailer failure, the AER has provided no evidence that this risk is present, let alone material. Further, no evidence is provided to highlight any specific weaknesses in the current prudential arrangements that support NEM settlements or the RoLR arrangements that manage the process of retailer failure.

It is more likely that any cash-flow pressures faced by retailers result in a more orderly restructuring or reconciliation of the retail sector. Retailer failure generally occurs when retailers are caught under-hedged through a period of high wholesale prices. In that case the immediacy of credit support requirements can force a business into administration with little warning. In this case, however, wholesale prices are down and this risk is low (or at least no different from usual). The gradual erosion of cash-flow and clear sight of network charges falling due should provide sufficient forewarning to manage any solvency issues in an orderly way, without overstretching the RoLR framework.

The AER also suggests that the introduction of the proposed rule would likely make retailers more likely to offer hardship arrangements or payment plans. Providing hardship assistance is already a legal obligation on retailers. No evidence has been provided that retailers are currently limiting access to such assistance during the COVID-19 health crisis. In any event, a more appropriate approach to achieve this ends, were it needed, would be to make temporary changes to the hardship framework, or for the AER to improve enforcement of existing hardship arrangements.

5.2 Costs

Introducing the proposed arrangements however would involve clear costs that would ultimately be borne by consumers. The costs arising from introducing arrangements for the deferred payment by retailers of network charges would include:

> cash-flow and consequential impacts on financing costs for network businesses
> potential costs associated with indirect impacts, such as the need for networks to review investment in transmission projects and consider reductions in staff, and
> the costs for all parties associated with the implementation and management of the arrangements.

The impacts on TransGrid (and similar impacts would be felt across networks) are set out in more detail in **Section 4.1** above. All of these impacts would ultimately be borne by consumers in one form or another. Consumers benefit from the financial stability engendered in networks under the current regulatory framework. The transfer of cash-flow risks to network businesses, and consequential cost implications, should not occur without clear identifiable benefits.