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Reference Code: RPR0016

23 June 2023

Review into the arrangements for failed retailers' electricity and gas contracts: Directions paper

AGL is pleased to provide our response to the *Review into the arrangements for failed retailers' electricity and gas contracts: Directions paper* (Directions paper) released by the Australian Energy Market Commission (AEMC) on 11 May 2023.

AGL operates nationally across the energy supply chain and delivers 4.2 million gas, electricity, and telecommunications services to our residential, small and large business, and wholesale customers across Australia. We operate Australia's largest electricity generation portfolio, with a generation capacity of over 11,000 MW, accounting for approximately 20% of the total generation within Australia's National Electricity Market.

AGL is registered as a default Retailer of Last Resort (RoLR) for both gas and electricity in various jurisdictions and in recent years has been the designated RoLR for several instances of retailer failure. Given these experiences, AGL is very supportive of the AEMC's review into the wholesale risks faced by designated RoLRs.

The AEMC's Directions paper has identified several ways to potentially reduce these risks and AGL strongly supports several of these options, primarily:

- in the retail electricity market:
  - improving the cost recovery mechanism for RoLR events, to ensure it allows for all the wholesale costs incurred by the designated RoLR;
  - allowing failed retailers to be billed for the cost of a RoLR event to both minimise the cost to consumers and discourage retailers from choosing to fail and enter the RoLR scheme; and
- in the retail gas market:
  - improving the gas directions framework so that all relevant gas contracts of a failed retailer are promptly accessible to the designated gas RoLR; and
  - extending the directions period to greater than 3 months to ensure the designated RoLR has access to gas supplies to service the transferred customers, especially in periods of short supply such as winter.

AGL's has provided more detailed responses to the questions raised in the Directions paper in Attachment A.

If you have any questions in relation to this submission, please contact Patrick Whish-Wilson on pwhish-wilson@agl.com.au.

Yours sincerely

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Attachment A: AGL Responses to the Directions paper

1. Reducing costs of electricity retailer failure

The designated RoLR can purchase electricity through the NEM to supply transferred customers however this energy will not be hedged in line with its current customer load or internal risk profile. There is a significant risk that the costs of energy procurement will exceed the RoLR' s revenue recovery from these customers. AGL believes this needs to be minimised.

Question 1: What improvements should be made to the RoLR cost recovery framework?

AGL believes that the costs claimable under the AER's cost recovery process should be explicitly specified to provide the designated RoLR some assurance that it can recover its costs. However, the specified claims will not be exhaustive as it must also retain the flexibility to include additional costs that may be relevant in the future.

The Default Market Offer (DMO) is the relevant reference price for any small customers in a RoLR event and it is likely that most costs inherent in the DMO are therefore relevant as claimable costs. Only network costs and industry fees and charges cannot vary despite market conditions. The cost recovery provisions should therefore define that any claimable costs must be determined by reference to the relevant cost allowances under the current DMO determination.

AGL also agrees that after a RoLR event, market costs should be recovered by the designated RoLR for the period of 9 months, as proposed in the Directions paper.

AGL believes that improving the cost recovery framework in this way will give certainty for the designated RoLR and should mitigate any issues with cashflow or accessing financial support. However, AGL does support that the cost of financing over such a period is claimable to ensure it is addressed.

Question 2: Should we issue the failed retailer with a bill for the costs of its failure?

AGL strongly supports the AEMC's proposal that after a RoLR event, a bill is issued to the failed retailer for any costs required under the RoLR cost recovery scheme.

This approach would:

- minimise the cost impact on consumers by potentially recovering costs through the failed retailer rather than through network costs to consumers;
- reduces the incentive for a retailer to voluntarily enter a RoLR event for commercial gain rather than because of insolvency; and
- have no readily apparent impact on a retailer's market participation and should therefore not require any minimum threshold to its application.

Of course, if the retailer was insolvent, the AER would only rank as an unsecured creditor and would likely receive little to no return on its bill through the insolvency proceedings. The AEMC proposed solution in the Directions paper is to make the AER a secured creditor by using the Personal Property Securities Register (PPSR). This approach is ingenious but unwieldy.

The difficulties of including the AER on the PPSR of every retailer are uncertain with complexities depending on their varied corporate structures and current debt provision already residing on the PPRS. AGL's view is this approach is unlikely to materially increase the rate of cost recovery from insolvent retailers and therefore the cost of implementing this process outweighs any benefits.

AGL also notes and agrees with the AEMC's proposed approach to continue to use the distribution network cost passthrough process to ensure timely recovery of costs. Allowing the designated RoLR to recover its approved costs promptly through DUOS charges is appropriate. Customers will be reimbursed when the failed retail has paid its bill and these funds are dispersed as a negative cost pass through in DUOS charges.

Question 3: What information is necessary for the AER and electricity RoLRs to fulfil their duties, and how should it be collected?

The designated RoLR requires a significant amount of information to effectively fulfill its RoLR duties. However, the amount of information varies considerably depending on the type of customer and fuel involved.

In the case of electricity RoLRs, provision of the full list of customers and NMIs provides access to much of the basic information on load, network tariff and meter type through MSATS.

However, for C&I customers, additional information on historical load shape and the customers' individual contract prices and terms is key. The additional load information should be able to be provided by the distribution networks.

2. Improving how gas retailer failures are managed.

In a gas RoLR event, the directions framework is supposed to provide the designated RoLR with access to the gas supply and pipeline contracts previously held by the failed retailer to help support servicing the transferred customers.

However, AGL's recent experience with the framework highlighted that the current directions are unclear and ineffective in addressing a significant gas RoLR event, to the detriment of the impacted customers. The gas directions framework therefore needs improvement so the risks faced by the designated RoLR and impacts on customers are minimised.

Question 4: Should we change the RoLR gas directions triggers?

The AEMC has recognised that the current directions framework is too focused on the physical availability of gas supply and questions whether additional triggers are needed. It also queries whether a materiality threshold is required.

AGL's recent experience was that the current trigger significantly delayed the AER making a direction under section 137 of the NERL. AGL's concern is that expanding the framework to include a set of triggers, and potentially including a threshold, is only adding further complexity to a process that needs to be fast and automatic given the urgency of a RoLR event.

Rather than using a trigger, AGL believes the gas directions framework need to be amended to allow all relevant gas supply contracts of the failed retailer to be utilised by the designated RoLR (at its election), so that they may provide the benefit of these gas supply contracts to impacted customers.

The AER gas directions should therefore be an unambiguous temporary 'novation' of all relevant gas contracts from the failed retailer to the designated gas RoLR. This should include any type of contract that is required to provide physical gas supply to these customers (eg. supply, storage, capacity and transport contracts).

AGL does not believe this regulatory change will adversely impact on retailers' ability to obtain supply contracts as gas producers will be largely unaffected by the direction.

However, AGL does recognise that in some instances, there may be unintended consequences for gas producers because of the temporary change in counter party but believes this in unlikely and can be mitigated by AER playing an intermediary role if necessary.

Question 5: Should we increase the length of time RoLR gas directions apply?

AGL believes that the gas directions should apply for longer than the current three-month period.

Every gas ROLR event will be different but, in most instances, the designated RoLR is likely to require the directed gas contracts to supply the transferred customers during the winter months, when gas supplies are at a premium. This means the actual timing of any retailer failure will be a significant factor in determining how long the gas directions are needed by the RoLR.

AGL expects that a period of 6 months would therefore mitigate the risks to the designated ROLR in most situations.

There may also be benefits to having some additional flexibility incorporated into the directions framework such as allowing the designated RoLR to apply to the AER for an extension of the directions in extenuating circumstances.

AGL is not concerned that a 6-month direction period will be too long in certain RoLR events as when the costs of the RoLR event are mitigated, AGL would expect any further benefits of the directed contracts to be distributed to the affected customers.

Question 6: Should we introduce negotiation principles? Question 7: Should we remove the negotiation process?

In AGL's experience, gas producers are willing to negotiate in good faith with a retailer during a ROLR event.

Therefore, the AEMC extending the gas directions period to 6 months will provide sufficient time for the designated RoLR to negotiate new contracts and removes the need for;

- the mandatory negotiation process in the directions; and
- any prescribed negotiation principles.

Question 8: How should we clarify what happens to contracts that begin or end during directions? Question 9: Should gas storage contracts be considered in the RoLR gas directions framework?

As highlighted above, AGL believes the AER gas directions needs to be automatic and allow the designated gas RoLR to use all relevant gas contracts of the failed retailer. This should include all type of contracts (supply, storage, capacity and transport) and should encompass any contracts that are due to commence in the directions period.

Similarly, any directed contracts that come to an end during the directions period should cease to be included in the directions.

If gas storage contracts are part of the failed retailers contracted supply, then they should naturally be included in the AER directions. This must include all of the relevant contracts for the storage product such as intake and withdraw rights, capacity on relevant pipelines and any gas in storage.

A RoLR event is most likely to occur in period of gas shortage or high gas prices so directing any gas storage contracts to a designated RoLR is likely to be pointless unless it includes the rights to any stored gas.

AGL accepts that there may be legal questions regarding the pre-purchased gas in storage and that the designated retailer may have to reimburse the failed retailer the cost of any gas it draws form storage. However, AGL believes this should only be the initial cost of the gas. Valuing this gas at a current market value may incentivise perverse behaviours by a failed retailer, prior to a RoLR event.

Question 10. How can the benefits or costs of RoLR events be shared with customers?

Under a framework where gas supply contracts are directed from the failed retailer to the designated RoLR, AGL supports having an obligation for any benefit of the supply contracts to be distributed amongst customers on a fair and reasonable basis.

AGL envisages this obligation being a high-level principle rather than any specific or detailed requirement as:

- the circumstances in relation to each RoLR event will be different; and
- the benefits of gas contracts are shared with other customers, not simply the customers that have been transferred. For example, providing the benefits of gas contracts to C&I customers will require lower default retail pricing which will benefit other C&I customers. It is a similar situation with small customers and the provision of standing and market offers.

As part of this obligation, AGL supports the RoLR advising the AER how it generally shared the benefits to meet this requirement.

Question 11. What information is necessary for the AER and gas RoLRs to fulfill their duties?

As highlighted above, the designated RoLR requires a significant amount of information to effectively fulfill its RoLR duties and this information varies depending on the types of customers involved. There is also additional information required in the case of a gas RoLR event.

In AGL's view, the designated RoLR should also have a clear right to access relevant information in a timely manner. The gas RoLR immediately requires:

- full list of customers;
- meter type;
- a copy of all gas supply contracts including transport and storage to determine which of the contracts it needs to utilise to best supply the customers;
- for C&I customers, the load, including ACQ, MDQ, historical consumption data (load shape) are also critical in order to forecast and nominate gas; and
- customer location to facilitate transportation requirements.

AGL would also highlight that additional information is needed to enable the RoLR to move C&I gas customers off the initial default prices as soon as possible. This includes:

- price and product information (eg. fixed price, pool price path through);
- Duration and term of contract;
- key contract terms and conditions; and
- credit history of customer.