Australian Energy Market Commission
GPO Box 2603
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Submitted on-line

Review Into the Arrangements for Failed Retailers' Electricity and Gas Contracts Directions Paper

Alinta Energy welcomes the opportunity to comment on the "*Review into the Arrangements for Failed Retailers' Electricity and Gas Contracts*" Directions Paper.

As an active investor in energy markets across Australia with an owned and contracted generation portfolio of more than 3,000MW and over 1 million electricity and gas customers, Alinta Energy has a strong interest in the policies and regulation governing the retail energy market and is well placed to provide comment on the consultation being undertaken.

As set out in our response to the consultation paper we understand that the AEMC's review has been prompted by the increased occurrence of retailer failures in the market during the recent unprecedented volatility in the wholesale market.

The protection of consumers through the Retail of Last Resort (RoLR) scheme is not at issue here; customers of failed retailers have received all appropriate protections, including the provision of uninterrupted energy supply during recent RoLR events. This demonstrates that the current RoLR scheme is functioning as intended by providing short term protections to customers during periods of high uncertainty.

The issue under consideration continues to be the cost implications for designated retailers in providing RoLR services and whether there are sufficient provisions to enable the recovery of reasonable costs associated with these services. In particular there is uncertainty surrounding which costs can be recovered, and the period over which they can be recovered.

In reviewing the arrangements for failed retailers' contracts, a more preventative approach should be considered that could lessen the risk of retailer failure. This would involve evaluating whether prudential requirements placed on entities seeking to enter the market are adequate.

Given the relatively low barriers to market entry, consideration should be given to whether the financial resilience assessment of new market entrants is currently set at a level commensurate with the obligations of energy providers in providing an essential service. A robust assessment process that ensures ongoing financial resilience of new entities, rather than relying on costly short-term protection schemes, holds the potential for greater efficiency.

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In addition, when a retailer does fail, provisions should be established to prevent directors of the failed retailer from re-entering the energy market for a prescribed period.

Our comments on the Directions Paper are focused on two key issues: the cost recovery mechanism for the RoLR and the proposal to bill the failed retailer for the costs of the RoLR scheme being enacted. Should you have any questions or wish to discuss any aspect of our submission I may be contacted on (02) 9372 2653 or via email: shaun.ruddy@alintaenergy.com.au

Yours sincerely

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Reducing costs for electricity retail failures

The directions paper raises the question as to what improvements should be made to the RoLR cost recovery framework. In particular there is a need for clarity regarding the costs that can be claimed by the designated retailer.

A RoLR should be permitted to recover the costs of providing RoLR services. To ensure efficiency and transparency, the recoverable costs should be clearly defined. Whilst the National Energy Retail Law currently sets out the costs that can be recovered, they are set at a high level, which may provide for a level of interpretive risk regarding which costs can and cannot be recovered.

Given the high probability of a RoLR event occurring during periods of elevated market conditions and using the Default Market Offer as a reference point for customer pricing, it is reasonable for a ROLR to recover the difference between the cost of supply and the relevant DMO costs when taking on customers. If the revenues received from the RoLR customers are below the cost of supply, the RoLR should be permitted to recover the shortfall.

In doing so, however, the RoLR would need to demonstrate, on an evidentiary basis, the cost recovery shortfall between its costs and the DMO. We would note the same principle would apply in the Victoria with the Victorian Default Offer.

Recovery of costs from the failed retailer

The Directions paper puts froward the option of recovering the costs of RoLR services from the failed retailer. However, the intent of making the failed retailer contribute to the costs of triggering the RoLR scheme is problematic.

As set out in the Directions paper, the likelihood of receiving payment from the failed retailer is influenced by two key factors; specifically, the nature of the retailer's failure, and whether they are solvent or insolvent at the time of the failure.

To address this issue, the paper suggests the radical solution of making the Australian Energy Regulator a secured creditor for the purposes of the RoLR scheme under the insolvency frameworks.

Alinta Energy strongly opposes his proposal. The AER is not a creditor, secured or otherwise, of any retailer under the RoLR scheme. Seeking to elevate the AER above other creditors that have legitimate claims against a failing retailer is not appropriate.

Furthermore, the proposal that the AER becomes a secured creditor, requiring all retailers to provide an all-assets security interest in favour of the AER on the Personal Property Securities Register, has wider implications for retailers and the market beyond the RoLR scheme.

Where a new, material, and unqualified financial risk is inserted into a business and imposed at a senior and secured level, it will significantly reduce the level of funding available to the business. In turn this will significantly increase liquidity risk, and at a minimum materially, negatively impact the ability of the business to access capital.

It would be prudent to consider the potential adverse impact of reduced liquidity across retailers/NEM market participants prior to any consideration being given to this proposal.

While a government secured interest in the assets of operators exists in some other regulated industries, we understand this has only been possible as:

a) the liability can be largely quantified/the risk attached assessed; and

b) that security is established at the conception of the business, so it is factored into the assessment by a borrower in setting up its capital structure, and its financiers in deciding to lend to it.

Notwithstanding these material issues, even if the proposal was feasible and the AER were to become a secured creditor:

- Higher capital costs across retailers would inevitably be passed on to consumers through higher energy costs, and far outweigh the benefit of any potential recovery of ROLR costs.
- The ability of the AER to recover costs will still be impacted by the type of retailer failure and the presence of any other secured creditors ahead of the AER in the wider insolvency process.

Given the complexities and breadth of issues associated with this proposal it should be discounted.