3 November 2023

Anna Collyer
Chair
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Submitted online at: www.aemc.gov.au

Dear Ms Collyer

Review of the Retailer Reliability Obligation – Draft Report

Origin Energy Limited (Origin) welcomes the opportunity to provide comments on the Australian Energy Market Commission's (AEMC) Review of the Retailer Reliability Obligation (RRO) Draft Report.

Origin is generally supportive of the draft recommendations, which we agree will assist with reducing regulatory burden for market participants and provide for improved customer outcomes while the RRO is in operation. Key recommendations in this respect include moving the T-1 Net Contract Position (NCP) compliance date to T and only requiring NCP reports to be submitted when operational demand during a reliability gap reaches the peak demand threshold; and providing the Australian Energy Regulator (AER) with a limited ability to revoke T-1 instruments if requested by the Australian Energy Market Operator (AEMO) in response an improved supply / demand outlook. Notwithstanding this, we have provided comments on additional issues the AEMC should consider in the development of the final report below.

As noted in our submission to the earlier Consultation Paper, we also do not consider the RRO to be an enduring mechanism for supporting reliability in the NEM, particularly given the progression of mechanisms like the Capacity Investment Scheme (CIS). We would therefore be supportive of the AEMC undertaking a self-initiated review of the overall policy efficiency of the RRO, taking into account new mechanisms that may overlap with the operation of the RRO.

Customer hedging arrangements

Origin offers a market-settled product which provides large customers with spot price exposure, along with the ability to fix a nominated MW volume of their load at a market rate, or use their own hedging arrangements, to manage their risk. The current RRO framework creates complexity / uncertainty for retailers in managing their liability for customers that utilise these types of products.

Customers can nominate to fix the price of a MW volume of their load at the market rate. Origin can then hedge its risk by offsetting the nomination with a purchase from the contract market. The AEMC should ensure it is clear in the NER and AER guidelines that only the hedge purchased by the retailer is to be captured in the retailer's NCP as a qualifying contract and no adjustment to the NCP is required for the contract with the customer. The arrangement with the customer could be interpreted as increasing the exposure of the liable entity to the volatility of the spot market and as such be required to be included in the NCP under NER cl.4A.E.2(c) and cl.4A.E.6(b)(7), notwithstanding the retailer has purchased a qualifying contract which offsets this exposure. This would be contrary to the intent of the RRO which requires liable entities to demonstrate they have entered sufficient contracts to cover their share of peak demand.

Customers may have also entered into their own hedging arrangements with a third party. For example, large customers may have agreements directly with financial institutions or renewable energy providers

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as a way to manage their Large-scale Renewable Energy Target (LRET) commitments and energy price risk. The current RRO framework does not allow the Financially Responsible Market Participant (FRMP) to include this contract in their NCP report, despite them being responsible for the customer load under the RRO.

In the above circumstance, to enable the retailer to purchase qualifying contracts to cover the customer's load without taking on significant exposure to the spot market, this potentially leads to a requirement on the customer to fix the price in their contract for any reliability gap period where a T-1 instrument has been made. This could ultimately result in the customer's load being over-hedged (as both the retailer and customer will have hedged the load), and therefore unnecessary costs.

Any resulting contractual arrangements which require the renegotiation of existing contracts when a T-1 instrument is made could be dissuading customers from pursuing innovative arrangements that support the transition to a two-sided energy market.

The complexity, compliance burden and potentially large civil penalties associated with the RRO create a significant barrier for customers voluntarily opting into the scheme. Given there appears to be no other mechanism to ensure all of a customer's hedges can be counted in an NCP, the AEMC should consider how this could best be addressed. If it is intended that a liable entity could enter into a pass-through arrangement with the customer to have the third-party contract counted in the NCP, then the firmness principles in the NER and the AER's interim contracts and firmness guideline should be reviewed to make this clear.

Related Entities

The RRO framework should allow liable entities which are also related entities to have their compliance assessed together. This would represent a minor framework change that reduces unnecessary compliance burden and better reflect the intent of the RRO.

The treatment of corporate groups is described in section 5.3.5 of the AER's contracts and firmness guidelines. A single corporate group with two registered participants is required to assign hedge contracts between them using inter-entity arrangements to match their expected peak load. This does not reflect how related entities approach contracting where risk is assessed in aggregate. It would be unreasonable to impose civil penalties on an individual liable entity that has not satisfied its RRO obligation where the related entities have complied in aggregate.

Allowing a liable entity to nominate a related entity in their NCP report would be a straightforward regulatory change with no risk of unintended consequences. This could also limit the compliance burden on opt-in customers looking to include third-party contracts as described in the previous section, with the compliance obligation (and associated penalties) falling on the nominated liable entity; although this would require the liable entity to have confidence in the opt-in customer's NCP report before accepting liability.

Opt-in timeframe

In moving the contract position date to T, consideration should also be given to moving the opt-in cut-off date to six months before the reliability gap to provide customers with additional time to consider participating in the RRO.

Any reduction in time between the opt-in date and the contract position date will need to consider the timeframe for the AER's decision to approve or reject the application. Section 3.4.1 of the AER's opt-in guidelines sets a target of 30 business days for this decision. This time limit should be prescribed in the NER as both the liable entity and opt-in customer require certainty of the outcome before making arrangements to comply with the RRO.

AER powers to revoke a T-1 instrument

The AEMC is considering a mechanism to enable a T-1 instrument which has previously been made to be cancelled on request by AEMO. We support this recommendation but consider a cut-off date should be established, such that a T-1 instrument cannot be revoked by the AER within three months of the beginning of the reliability gap period.

Three months provides sufficient opportunity for the T-1 instrument to be cancelled if supply / demand conditions change and a reliability gap is no longer forecast leading up to T, but gives a clear point in time where liable entities have certainty that the T-1 instrument will be in effect. It is also important for any time limit to reference the AER's decision rather than AEMO's request to cancel an instrument to provide a firm go/no-go date to take action and finalise any arrangements.

Firmness principles

If the recommended change to the contract position date is made, liable entities will be finalising their bespoke methodologies after the reliability gap period has ended. The current wording of the firmness principles in the NER will need to be reviewed to retain alignment with how the RRO is intended to operate in this context (i.e. to provide a forward contracting signal).

For example, principle 4A.E.3(a)(2)(iii) specifies that a firmness factor applied to a qualifying contract will take into account “the *likelihood* of the qualifying contract providing cover to the liable entity during the gap trading intervals”. Consistent with this, the firmness factor applied to a generator for the purpose of quantifying the expected cover it will provide would rely predominantly on historical performance data. However, following the reliability gap period, the *actual* availability of the generator during the reliability gap period would be known. It will be important to clarify how the performance of a generator close to T is expected to inform the calculation of firmness factors. It would be a perverse outcome if an unplanned outage (or other similar event) leading up to, or during, a reliability gap period could unduly impact a generators firmness factor, potentially exposing the liable entity to civil penalties. The overarching firmness principles and associated guidelines should therefore ensure that firmness factors under bespoke methodologies can continue to be based on expected generator performance during similar historical periods, and not be disproportionately weighted toward actual performance at T.

Market Liquidity Obligation (MLO) liquidity period

The MLO market making requirements currently end at the T-1 cut-off date, aligning with the contract position date. If the contract position date is moved to T there is an opportunity to extend the MLO window beyond T-1 in cases where a T-1 instrument is made. However, given liquidity generally increases as the period approaches and MLO providers will need to manage their own positions, we do not consider it necessary / appropriate to materially extend the MLO period. At a minimum, MLO obligations should not extend to within six months of the contract position date.

If you wish to discuss any aspect of this submission further, please contact Ben Hayward on 03 9067 3403.

Yours Sincerely,

S Cole

Shaun Cole
Group Manager, Regulatory Policy