Ergon Energy Corporation Limited
and
Ergon Energy Queensland Pty Ltd

AER Retailer Authorisation – Issues Paper and Draft Guideline

Australian Energy Regulator

30 April 2010

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This submission, which is available for publication, is made by:

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1 INTRODUCTION

Ergon Energy Corporation Limited (EECL) and Ergon Energy Queensland Pty Ltd (EEQ) welcome the opportunity to provide comment to the Australian Energy Regulator (AER) on its *Retailer Authorisation Guideline: Issues Paper* (Issues Paper) and *Retailer Authorisation Guideline: Draft for preliminary consultation* (Guideline).

This submission is provided by:

- EECL, in its capacity as a distribution network service provider in Queensland; and
- EEQ, in its capacity as a non-competing area retail entity in Queensland.

In this submission, EECL and EEQ are collectively referred to as 'Ergon Energy'.

Ergon Energy has structured this submission in two parts:

Part A: Ergon Energy's responses to questions raised in the Issues Paper.

Part B: Ergon Energy's general comments on the draft Guideline.

Ergon Energy is available to discuss this submission or provide further detail regarding the issues that it has raised, should the AER require.

2 PART A – RESPONSE TO THE AER'S QUESTIONS

Process for assessing retailer authorisations

3.1 Would prospective applicants benefit from briefings prior to the submission of an application? If so, please provide details of the form (for example, group or individual sessions) and content of briefings that would be most beneficial for prospective applicants.

Ergon Energy considers that individual, informal briefings sessions would be beneficial to applicants and should be available upon request. Group sessions are unlikely to prove workable on the basis that:

- the timing of applications for authorisation would be difficult to judge and are unlikely to coincide; and
- retailers would be expected to have concerns regarding confidentiality when discussing the information to be provided in support of the entry criteria.

The content of the briefings should follow the questions and requirements in the application for authorisation and Guideline. That is, the briefings should clarify, not replace, the information contained in the application for authorisation and Guideline. Over time, briefing sessions should become more infrequent as the application and Guideline are refined in response to questions raised during briefing sessions and the application process more generally.

Entry criteria and information requirements

4.1 Is it appropriate for the AER to require only a compliance strategy rather than a compliance plan or systems at the time of the application? Please provide any reasons for your view.

Ergon Energy believes that an application for authorisation should be supported by a compliance plan. In developing a compliance plan, applicants would be prompted to consider how the risks and responsibilities associated with becoming a retailer will be met. In particular:

- satisfaction of settlement and prudential obligations to the Australian Energy Market Operator (AEMO) and the payment of network charges and credit support to distributors; and
- the ability to deliver market compliant systems in the key areas of billing, call centre and market interactions (e.g. MSATS and B2B capability).

The compliance plan should identify any constraints or limitations in the applicant's organisational and technical capacity or financial resources. For example, with respect to the ability to deliver market compliant systems, if the backend systems proposed to be utilised by applicants would not initially be fully automated then applicants should provide details of any constraints placed on manual processing of transactions and detail a timeframe of expectations of full compliance.

Ergon Energy accepts that requiring applicants to have a full compliance system in place at the time of application may be costly, particularly since the compliance system would become redundant should the application not be approved. The ability to rapidly establish a compliance system prior to the commencement of retail activities should however be demonstrated.

4.2 What guidance, if any, should the guideline provide on the types of risks that the AER would expect to be covered by a risk management strategy?

The Guideline should provide examples of the risks that retailers face so that prospective retailers are reasonably informed. These include:

- customers delaying or defaulting on payment for electricity consumed;
- an inability to purchase adequate wholesale electricity contract cover (i.e. in terms of volume or price) and the management of high and prolonged pool price events where there is spot market exposure;
- the failure of key information technology and communication systems, such as billing, customer management systems, the interface with MSATS, and the B2B e-hub;
- loss of key personnel; and
- fraud or material negligence by staff.

Applicants should demonstrate through the application that the risks are understood and that they are addressed through the compliance strategy and compliance plan. For example, that the risk profile is tailored to the retailer's market entry and customer acquisition strategy.

4.3 Is 12 months an adequate period for the assessment of whether a retailer has the financial capacity to operate without reliance on customer takings? Please provide any reasons for your view.

Ergon Energy believes that any assessment of financial capacity should have close regard to the:

- retailer's market entry and customer acquisition strategy (e.g. number of customers and load); and
- risks identified in the Guideline (e.g. high and prolonged pool price events), which are addressed though the retailer's compliance strategy and compliance plan.

There should be a notification mechanism (e.g. event-based reporting) through which the retailer advises the AER of changes in its financial standing (e.g. the acquisition of customer load materially higher than that envisaged under its market entry strategy) and confirms its ongoing financial integrity relative to the change in circumstance.

4.4 The AER acknowledges the limitations of financial statements and declarations in establishing an applicant's financial health. What alternative methods of assessment may be appropriate?

Ergon Energy suggests that the AER could examine prospective retailers':

- credit ratings; and
- the current relationship and financial health of parent and subsidiary companies.

4.5 Does the limitation on information that needs to be provided on compliance breaches—being those that have occurred in the past 10 years and that have led to enforcement action or an enforceable undertaking—strike an appropriate balance between ensuring a rigorous assessment and the information burden on applicants? Please provide any reasons for your view.

The time period for retention of taxation and business records is five to seven years and the period that a person is declared bankrupt ranges from three to eight years. Therefore, Ergon Energy believes that the proposed period of 10 years for providing information on compliance breaches is appropriate.

4.6 What issues or concerns may arise from a requirement for applicants to provide certified criminal history checks?

Ergon Energy can see no issues or concerns with this requirement. Criminal history checks are commonly required to support authorisations in the financial services industry, including the appointment of Responsible Managers under an entity's Australian Financial Services Licence.

Comparable checks should also be obtained from authorities in countries where the applicant or key personnel have resided for a significant period during the past 10 years.

4.7 What other information requirements not provided for in the draft guideline would be appropriate for the AER to impose? Please provide details of these requirements and the rationale for inclusion.

Please refer to section 3 of this submission.

4.8 Which, if any, of the information requirements contained in the draft guideline seem unnecessary or unduly burdensome? Please provide details and the reasoning behind your comments.

Ergon Energy does not believe any of the information requirements contained in the Guideline seem unnecessary or unduly burdensome.

Issues subsequent to the grant of a retailer authorisation

5.1 Is it appropriate to target retailers who wish to begin or resume retailing after a period of dormancy for compliance audits or monitoring? Please provide any reasons for your view.

Ergon Energy believes it is appropriate for the AER to have an increased focus on auditing and assessing the compliance of retailers who begin or resume retailing after a period of dormancy. A retailer's circumstances may have changed in the intervening period and regulatory requirements, market systems and processes are constantly evolving.

5.2 What matters should the AER have regard to, other than the rights of customers, when imposing conditions on the transfer, surrender or revocation of a retailer authorisation?

The AER should have regard to whether the 'new' retailer (i.e. accepting the transferred customers):

- has the financial capacity, organisational and technical expertise and the personnel, necessary to service the transferred or surrendered customers, in addition to its own customers. Particular regard should be had to the impact of the transfer on the new retailer's financial position and management of risk; and

- will be provided with, or have unhindered access to, customer data, including customer contracts (terms and prices). This information will be crucial to the management of risk, by allowing the new retailer to efficiently transfer the customer, issues bills and manage its wholesale market exposure.

Ergon Energy agrees with the requirement that the reasons for the transfer, surrender or revocation of a Retail authorisation be stated as this will guide the AER as to whether to approve the transaction.

5.3 What issues may arise, if any, in requiring the holder of the retailer authorisation to demonstrate that customers will remain on the same or better terms following a transfer or surrender of the retailer authorisation?

A new retailer should not be penalised by a requirement to provide customer retail services under unprofitable market contracts, for example in circumstances where the terms and conditions (including as to price) of the original retailer's market offering contributed to its demise.

The AER will also need to ensure that the Guideline and any conditions attached to the transfer do not adversely impact pricing arrangements and cost recovery for transfers that occur pursuant to the Retailer of Last Resort (ROLR) regime.

5.4 Is it appropriate for the AER to require applicants to develop procedures for customers to take action against them following the revocation or surrender of the retailer authorisation? If not, what other protections for customers are / could be provided?

Ergon Energy believes that, for small customers, this is a matter that is more appropriately addressed through the membership requirements of jurisdictional Ombudsman Schemes. For example, under the Energy Ombudsman Act 2006 (Qld):

- section 18(2) permits a dispute to be referred to the Energy Ombudsman even if an entity has ceased to be a retailer; and
- section 64 provides that if an entity stops being an retailer, it continues to be a member of the Energy Ombudsman Scheme for a period of 12 months.

Large customers who fall outside the coverage of the jurisdictional Ombudsman Schemes, can pursue commercial remedies against the retailer through the legal system.

3 PART B – GENERAL COMMENTS

Ergon Energy has the following comments on the proposed Guideline:

- **Part 1: AER process**

This section should state that any fees for retailer authorisations will be contained in the National Energy Regulations, consistent with section 1101(4) of the National Energy Retail Law.

- **Section 2.1: Organisational and technical capacity criterion**

It is suggested that the information requirements should be expanded to include a requirement for the applicant to evidence its ability to meet third party financial commitments, including the payment of network charges and credit support. This would be consistent with the requirement to provide evidence of prudential arrangements under Item 20 of the information requirements.

- **Section 2.2: Financial resources criterion**

Section 2.2 of the Guideline states:

> *Our assessment of financial viability is a one-off entry test designed to satisfy us that an applicant's retailer authorisation application should be approved. It should not be relied upon as an indication of a retailer's ongoing financial viability or profitability.*
>
> *It is not the AER's role to make ongoing financial assessments of a retailer's financial viability or provide comfort about the financial capacity of retailers that have commenced operations. Ongoing prudential assessments are undertaken by AEMO to ensure retailers have sufficient financial capacity to operate in the relevant wholesale markets.*

The question of a retailer's financial capacity extends beyond a retailer's satisfaction of its prudential obligations to AEMO and includes financial obligations to other parties, such as the payment of network charges and credit support to distribution network service providers under proposed amendments to the National Electricity Rules. Ergon Energy believes that the AER should have close regard to the retailer's ongoing satisfaction of these and other relevant financial obligations as part of its monitoring and compliance program.

- **Section 2.3: Suitability criterion**

It is suggested that Item 6 of the information requirements should be expanded to include senior personnel holding key financial positions within the applicant (e.g. Chief Financial Officer and Trading Manager). This information should be provided upon request.

- **Section 3.1: Revocation**

Ergon Energy does not believe that it is appropriate for the Guideline to stipulate that customers that have not been transferred to another retailer by the date that the revocation takes effect will become customers of the local area retailer. This pre-empts the outcome of the process for the appointment of ROLRs outlined in Part 6 of the 2nd Exposure Draft of the National Energy Retail Law.

In relation to the processes for revocation, Ergon Energy also recommends that:

- the written notice of intention to revoke should clarify whether the proposed revocation applies to the retailer's activities in all, or only some, jurisdictions; and

- the statement:

  > *We will inform AEMO of the decision.*

  should be amended to

  > *We will inform AEMO and distributors (where the retailer and a distributor have shared customers) of the decision.*

  It is important to ensure that distributors (who are financially exposed to retailers with respect to the payment of network charges) are aware of relevant events when conducting dealings with retailers. An event culminating in the revocation of an authorisation will not always be a ROLR event, for which the distributor receives a separate notification.

- **Section 3.3: Surrender**

Ergon Energy recommends the inclusion of the following information requirement in an application for surrender:

> *Documentation demonstrating that appropriate arrangements have been made to fully satisfy all outstanding financial commitments to market institutions, regulatory bodies and distributors.*

This is intended to ensure that a retailer has complied with all financial obligations, including. settlement obligations and the payment of network charges.