30 April 2010

General Manager
Markets Branch
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Email: AERInquiry@aer.gov.au

Dear Sir/Madam,

RE: RETAILER AUTHORISATION GUIDELINE- ISSUES PAPER

Origin appreciates the opportunity to comment on the Australian Energy Regulator's (AER's) Retailer Authorisation Guideline Issues paper and we recognise that this is a preliminary consultation and that a full formal consultation will occur upon passage of the Retail Law.

Origin notes the AER's comments that arrangements for transition from existing jurisdictional licenses to national authorisations are not covered in the Issues Paper. However, it is understood that existing retailers will not be required to re-apply for their authorisations, and so we assume that this exemption will form part of a separate set of transitional law and rules.

The AER's draft retailer Authorisation Guideline as proposed is generally supported because it:

- Places the responsibility on organisations to prove they have the fundamental technical, financial and risk management capability to become a retailer of energy; and
- Proposes that organisations should substantiate their suitability as retailers; the failure of a retailer can have significant consequential impacts on both customers and other market participants. The ongoing viability of the energy market should be the foremost consideration when contemplating the criteria for new entrants into the market. The fact that the National Electricity Market (NEM) has encountered two retailers of last resort events in recent years has elevated the importance of retailer viability when assessing the value that new entrants bring to the market.

Specific responses to the questions raised in the Issues Paper

1. *Process for assessing retailer authorisations (Issues Paper Section 3)*

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.

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Origin supports the concept of briefings by the AER to explain their expectations to prospective retailers. These briefings should remain confidential between the AER and prospective retailers so that there is open discussion where clarity can be sought in detail by the proponent retailer and the AER can be forthright in outlining its expectations with regard to authorisation requirements.

The briefings can also provide to parties contemplating entering the retail market a greater understanding of the risks of the market and the need for appropriate investment in risk management and customer management systems and processes.

2. *Entry criteria and information requirements (Issues Paper Section 4)*

> *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.*
>
> *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?*
>
> *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.*

It is reasonable to expect that a party applying for a retailer authorisation will have considered how it plans to manage compliance and the systems it will adopt. A compliance strategy could be very high level and not necessarily detail the mechanics of implementation. Therefore, both a compliance strategy and a plan should be provided at this high level of detail, with the understanding that:

- a flexible approach may be appropriate where the retailer is a small start-up operation; however
- The fundamental obligation to comply with the Regulatory instruments remains – a retailer's size is not an excuse for non-compliance with fundamental consumer obligations.

A core capability of energy retailing is risk management and any new entrant retailer should be well aware of the risks that it may encounter. The AER should not need to list the risks in the guideline (although they may be addressed in the proposed "briefing" sessions). Rather, the AER should see the proponent's risk management strategy response as a key indicator of its capability. From an energy cost perspective the AER should be satisfied that a proponent's wholesale market risk management strategy is sufficiently robust to ensure the market is not likely to be exposed to a retailer default and that it is suitably scalable to match the proponent's customer acquisition strategy. The risk management strategy should also satisfy the AER that the proponent can sustain a reasonable period of exposure to maximum wholesale energy prices [Value of Lost Load (VOLL)].

The assessment of a proponent's financial capacity should be broader than simply judging the proponent's ability to operate for 12 months without relying on customer takings. The financial assessment should entail a holistic view of the organisation and take the following into consideration, at a minimum:

- The 5 – 10 year business plan prepared by the proponent retailer;

- Company structure;
- Financial statements – current balance sheet and financial data;
- Statements of assets and liabilities;
- Guarantees in place;
- Ability to meet Australian Energy Market Operator's (AEMO) prudential requirements;
- Ability to meet distributors' credit support arrangements in the applicable jurisdictions;
- Wholesale risk management strategy;
- Operational structure;
- Customer acquisition plan; and
- Revenue assurance and debt management plan.

The proponent's business plan should indicate the target rate for customer growth (and customer segments[1]) and how the proponent will meet increased credit support requirements from AEMO and distributors and the increasing operational and wholesale energy costs of servicing a growing customer base. The risk management plan and the proponent's ability to fund growing capital requirements are also fundamental in determining the financial viability of a proponent retailer.

The importance of the initial assessment of a retailer authorisation application should not be underestimated; once the retailer acquires customers an authorisation revocation has significant impacts on market participants and customers. Moreover, once an authorisation has been granted, the AER's role is limited to managing compliance breaches by the various enforcement measures to remedy any shortfalls in the retailer's operation.

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?

4.5 Does the limitation on information that need 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.

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

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.

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.

[1]For instance the credit risk for some customer segments can be much higher than others as credit security options may or may not be regulated.

Origin confirms the AER's concerns with the limitations of "financial statements and declarations" as indicators of a business's ability to operate in the energy retail market. Given the risks to other market participants it is important for the AER to investigate alternative and/or complementary measures. In addition, it is important to consider the financial statements in the context of the business plan, for instance, whether the cash reserve is sufficient to support the planned growth in customer numbers, given the parallel prudential, marketing and working capital requirements of an energy retailer.

Origin agrees with the AER that it is critically important that the holder of a retail licence is a suitable person to retail energy to consumers. In determining the suitability of a particular applicant the AER's task is to make an objective evaluation of the ability of the entity to fulfil its obligations as an energy retailer. In determining this, it is appropriate for the AER to consider the way in which the applicant conducts its current enterprises and intends to conduct a business retailing electricity to consumers.

It is neither appropriate nor necessary for the AER, as an energy regulator, to have the power to compulsorily require a wide range of people connected with the applicant to disclose highly sensitive personal information about themselves in order to determine whether the applicant, which is a commercial entity, can retail electricity. The disclosure of such personal information to the AER will do nothing substantive to assist in protecting consumers and the participants in the National Electricity Market from the risk that the holder of a retail licence will fail. To the contrary, it could potentially deter qualified persons who could make a valuable contribution to the operation of a retail business from doing so in order to avoid having personal information about themselves disclosed to the AER to use as it sees fit. In short, the proposal seems to be little more than a fishing expedition by the AER to see whether it uncovers anything of interest (relevant or otherwise to the question of whether the applicant should be authorised to retail energy) about persons associated with the applicant.

Notably, the proposal makes no attempt to target either the people whose individual decisions could relevantly impact the applicant's conduct or the type of criminal conduct that could impact on the operation of a retailing business. For example:

- There is no limitation on the type of criminal conduct about which information is sought or attempt to link it to the type of dishonest or fraudulent behaviour which could possibly properly be of concern to the AER. Conduct such as disturbing the peace or traffic offences would have to be disclosed;

- There are no specific safeguards limiting the use the AER can make of the information and so preventing it from using the information for a more general purpose as contemplated by section 814 of the National Energy Retail Law (2nd Exposure Draft) including disclosing it to any other government agency;

- There are no specific safeguards requiring the AER to disregard any information included in any criminal history check performed by the Australian Federal Police (or otherwise) regarding spent convictions (which may not always be removed from the relevant Police criminal history system); and

- The category of persons who may be subject to requests is not limited to people whose individual actions could materially impact on the way in which the applicant conducts its retail business. The only people who may be in such a position are the senior managers in such a business. Directors of the applicant (let alone directors of the holding company of the applicant) are highly unlikely

as individuals to be in such a position given the collegial decision-making framework in which they perform their duties. People whose sole association with the company with ownership of 20% of the shares are even less likely to be in this position. It is unnecessary and inappropriate that such people be subject to mandatory disclosure of sensitive personal information about themselves.

Under item 2.1 Organisational and Technical Capacity Criterion on page 10 of the draft Retailer Authorisation Guideline reference is made to the requirement for a retailer proponent's employees to be trained to "*identify hardship customers and appropriately manage issues related to hardship customers*". Origin recognises the importance of developing skills in the management of customers in hardship, but would reiterate in this context that the only practical way to "identify hardship customers" is for the customer to self-identify. In Origin's view, a retailer should only be required to train staff to work effectively with customers who self-identify as being in hardship. This requirement needs to be amended.

3. 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.*

Origin seeks clarification as to whether this requirement could apply to a retailer active in several jurisdictions but seeking to resume retailing activity in one jurisdiction where it has been inactive. Origin does not believe that any compliance audits or monitoring should be necessary in this instance. One benefit of a national regime ought to be that a retailer meeting its requirements in one jurisdiction can be assumed to be capable of meeting them in all jurisdictions. For Origin, this is a primary benefit of a national regime.

However, in the instance where the retailer has withdrawn from all markets, then it may be appropriate to undertake a more substantive review prior to their commencement. The extent of this may need to reflect the basis of the retailer's withdrawal from the market, for instance if this had occurred as part of a RoLR event.

> *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 ongoing viability of the market and other market participants must be a key objective of the AER when considering the rights of customers under these conditions. As several second tier retailers now have greater than 50 000 customers a surrender or revocation of authorisation for these retailers would need to be managed carefully, particularly if it occurred during a peak energy consumption period.

A key success factor in this process would be the completeness and accurate transfer of customer data between the various parties involved. There should also be a responsibility on the withdrawing party to provide compliant information to the third parties including ensuring that for instance, customer detail notifications are up-to-date.

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?

In the event of an acquisition, broadly speaking, customers on market contracts would be likely to have their contracts assigned, while customers on standard contracts would continue to enjoy the same conditions – so the bulk of these customers would remain on terms very similar or identical to those they were on prior to the transfer.

It is unnecessary for the Guideline to stipulate that the customers should remain on comparable or better conditions as this is managed by contract law. And such an obligation may hinder the orderly transfer of customers through sale/acquisition and promote the alternative of a RoLR event, as it may not be even possible for another retailer to offer the exact terms, or to quantify what is a "better condition" (for instance, retailers have quite differently structured "green" offerings – how could they be compared?).

Importantly, all the relevant markets have high levels of competition, and customers who are dissatisfied with the transfer under a sale, can readily seek out other market offers more attuned to their preferences.

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?

The revocation of an authorisation would most likely trigger a retailer of last resort (RoLR) event and in this context the key objective for the market is to ensure that customers continue to receive a supply of energy on fair and reasonable terms. RoLR provisions will ensure that this occurs. The ongoing management of customer contractual issues with the failed retailer would be best managed under existing corporate and commercial laws.

The establishment of separate procedures for energy customers to take action against a failed retailer would probably never be able to be funded or implemented as the insolvency practitioner has administrative control over an insolvent company and is bound by insolvency law obligations. In the event of authorisation surrender the transferee retailer has the obligation to manage outstanding contractual issues with the customer so there is also no need for additional procedures.

Should you have any questions regarding this submission please do not hesitate to contact Randall Brown on 03 9652 5880.

Yours sincerely

B J Hughson

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Regulatory and Relationships Manager