SUBMISSION

EUAA
Energy Users Association of Australia

ALLOWING AEMO TO ACCEPT CASH AS CREDIT SUPPORT CONSULTATION PAPER.

ERC 0403

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INTRODUCTION

The Energy Users' Association of Australia (EUAA) is the peak body representing Australian commercial and industrial energy users. Our membership covers a broad cross section of the Australian economy including significant retail, manufacturing, building materials and food processing industries. Combined our members employ over 1 million Australians, pay billions in energy bills every year and in many cases are exposed to the fluctuations and challenges of international trade.

Thank you for the opportunity to make a submission to the "Allowing AEMO to accept cash as credit support" rule change Consultation Paper (Consultation Paper).

We would like to disclose that the rule change proponent Delta Electricity, is a Supporting Member of the EUAA. We have spoken to Delta Electricity about this rule change, but they have not sought to influence our response. Our response is based purely on the needs of the many energy users represented by the EUAA and guided by the National Electricity Objective (NEO).

Like most of our financial institutions, a majority of EUAA member companies have made commitments to net zero by 2050 along with having strong ESG targets. This requires steady progress towards decarbonising their energy intensive operations over the coming decades. However, they realise this will be a long and expensive process and that at times the path to achieving these goals will be littered with unexpected obstacles and seemingly insurmountable challenges. This is why they take a pragmatic approach to the decarbonisation challenge, maintaining a high degree of flexibility in their approach so as to maintain the health of their core business, which in most cases funds the technological transformation to achieve net-zero.

We have seen state governments take similar actions in recent years by extending the operational life of thermal generators in Victoria (Yallourn twice) and most recently in NSW (Eraring). If state governments with strong commitments to net zero can make these pragmatic decisions to maintain security of supply on behalf of consumers it is puzzling why financial institutions can't or won't do the same leaving AEMO and market participants to rapidly respond in order to maintain secure electricity supply.

The EUAA supports the transition to a net zero energy system but recognise the challenges in achieving this target in a way that maintains energy reliability at least cost to consumers. In seeking to accelerate quickly to this goal, the Federal Government has an ambitious target of achieving 82% renewable energy by 2030. However, it is clear that a range of factors are impacting our ability to meet this target.

This will likely result in three things:

- we will reach the target later than planned
- we will not have sufficient capacity installed to replace retiring plant and
- we will need to extend the life of some existing thermal assets to maintain supply reliability

With this situation looming large over the NEM, we require all generating assets to be available when required by AEMO, so they can maintain security of supply and minimise the likelihood of serious prices shocks. It would be reckless to allow a situation where a key generating asset is unable to make a vital contribution to maintaining security of supply over the coming years.

Therefore, the EUAA support the rule change request to allow AEMO to accept cash as credit support.

RESPONSE TO CONSULTATION PAPER QUESTIONS

Question 1: Do the current available options for credit support create problems in the NEM?

- How likely is it that other participants may face issues in the future obtaining bank guarantees or letters of credit, similar to the issues currently faced by Delta or otherwise?
- Could the current options for credit support create risks to the supply of electricity? Are these short-term risks or longer-term risks to the broader NEM?
- Are there any other issues faced by market participants due to the current options to provide credit support?

EUAA Response

As a stand-alone, non-government thermal generator Delta Electricity appears to be in a unique position as they do not have a large, diversified portfolio of assets or a state government to stand behind them. So, while this rule change would likely just impact them today, we can see a situation where others may find themselves in this situation in the future. The most obvious would be new market participants seeking to develop the 15GW of gas fired peaking plant that AEMO has identified as required to maintain energy security and reliability in a VRE dominated NEM.

The impact of not allowing more flexible prudential arrangements include:

- Serious immediate risks to stable supply of electricity. In the case of Delta Electricity, immediate risks to supply and system services like inertia and system strength, will arise if they are forced to withdraw capacity before sufficient replacement assets are in place (including assets the provide MWh, dispatchable capacity and system services).
- Serious medium to long-term risks to stable supply of electricity if the timely deployment of sufficient gas fired peaking plant is compromised.
- In addition to serious risks to stable supply of electricity supply, if more flexible prudential arrangements are not in place then the ability of new market entrants would be compromised which in turn would lead to less competition and potential concentration of market power into the hands of a small number of vertically integrated market participants.

Question 2: What are the potential benefits of allowing cash to be provided as credit support?

- What benefits do you consider there to be from allowing cash to be provided as credit support?
- If there are benefits, how material could they be?

EUAA Response

We are observing an energy transition that is becoming increasingly ”bumpy” and unpredictable. In these circumstances more flexibility is required, not less, to ensure the interests of consumers are met. Allowing cash to be provided as credit support in specific circumstances provides market participants who are facing unique circumstances to continue to make a vital contribution to the security of electricity supply and reduce the likelihood of prices shocks for consumers.

Question 3: What are the potential costs of allowing cash to be provided as credit support?

- What are your views on risks to AEMO and markets participants from insolvencies if cash is provided as credit support? Are these risks sufficiently material to outweigh any benefits of the proposal?
- What do you consider would be the likely impact on emissions by allowing cash to be provided as credit support?
- Are there any other potential costs from allowing cash to be provided as credit support?
- If there are costs, how material are they?

EUAA Response

We do not have a strong view on the risks to AEMO from insolvencies if cash is provided as credit support. However, conversations with various market participants would suggest that this is not an insurmountable problem. In the case of Delta Electricity, we view the risk of insolvencies and therefore the risk of higher costs on consumers from socialisation of AEMO risk as a result of an insolvency event to be far less (but not zero) than the risk to reliable electricity supply and prices shocks to consumers if capacity is forced to withdraw from the market before the market is ready.

We do not see that this rule change would have a negative impact on emissions (i.e. emissions would not be greater than they otherwise would have been) as there is no indication that this rule change would extend the life of the Delta Electricity asset beyond its current scheduled retirement date. This rule change is about making sure that Delta Electricity continues to provide reliable energy up until it’s scheduled retirement date.

Some may argue that prematurely forcing Delta Electricity from the market would reduce emissions. We are not convinced of this as other dispatchable generation would need to be engaged to maintain energy supply. This would include greater output from other thermal generation including diesel generators, forcing emission higher in the short to medium-term.

Question 4: Are there any provisions that could enable AEMO to sufficiently manage insolvency risks when accepting cash as credit support?

If cash is accepted as a form of credit support, do insolvency risks to AEMO and the market need to be managed? If so, could risks be satisfactorily managed by:

- socialising costs from cash clawbacks among market participants, instead of AEMO bearing the costs?
- guidance to AEMO on conditions for which cash could be provided as credit support?
- AEMO registering a security interest in the cash on the Personal Property Securities Register?

EUAA Response

We do not have a strong view on the risks to AEMO from insolvencies if cash is provided as credit support. However, conversations with various market participants would suggest that this is not an insurmountable problem. Additionally, the Consultation Paper offers a number of mitigating options available to them, in particular the reference to the existing WEM arrangements where cash is accepted as security[1].

In the case of Delta Electricity, we view the risk of insolvencies and therefore the risk of higher costs on consumers from socialisation of AEMO risk as a result of an insolvency event to be far less (but not zero) than the risk to reliable electricity supply and prices shocks to consumers if capacity is forced to withdraw from the market before the market is ready.

Question 5: Would transitional rules be needed?

We note that Delta's current bank guarantee facilities are expiring at the end of 2024.

If a rule was made to allow AEMO to accept cash as credit support, would transitional rules be needed to enable Delta or other participants to provide cash as credit support during an interim period? If so, what would be an appropriate form of transitional rules?

EUAA Response

We hope that the rule change can be completed by the 31st December when the bank guarantee currently provided to Delta Electricity expires. Clearly if this is not the case then transitional arrangements would need to be put in place which may include some interim support provided by government to AEMO to ensure supply reliability. We believe there would be strong energy security and NEO related arguments for this. This support would be withdrawn once alternative arrangements that this rule change contemplates are in place.

Question 6: Are there any additional variations or alternative options to Delta's proposal?

Do you have any additional variations or alternative options to Delta's proposal that may address problems associated with the available options for providing credit support in the NEM?

EUAA Response

Given AEMO prudential requirements are quite specific there does not appear to be many options available other than what Delta Electricity has proposed. The only alternative would be for government (state or federal) to provide credit support in the interests of maintaining supply reliability and avoiding prices shocks. (This may be required as part of transitional arrangements as discussed previously).

[1] Consultation Paper Page 10.

The Queensland Treasury essentially provide credit support for state owned generators in that state. The NSW government has provided a degree of underwriting support for Origin's Eraring plant that facilitated an extension of its closure date. The arrangements between the Victorian Government and Yallourn are commercial in confidence so we can't speak to the nature of those arrangements.

The Federal Government are underwriting new investment via the CIS as have numerous state governments via CFD arrangements. While these mechanisms are more revenue support than credit support they are still using taxpayer dollars (via Treasury balance sheets) to provide private entities with a financial instrument to manage risk. It could be argued that providing credit support poses less of a risk to taxpayers than underwriting revenues that are far more volatile in nature.

Question 7: Assessment framework

Do you agree with the proposed assessment criteria? Are there additional criteria that the Commission should consider, or criteria included here that are not relevant? What are stakeholders views on the costs and benefits of the proposed solution or alternative options against these criteria?

EUAA Response

The EUAA are in general agreement with the assessment framework, based as it is on the National Electricity Objective (NEO)

In making this rule change the NEO must be the guiding force that finds a correct balance between its many elements. Some may argue that prematurely forcing Delta Electricity from the market would reduce emissions and therefore satisfy part of the NEO. We are not convinced of this as other dispatchable generation would need to be engaged to maintain energy supply. This would include greater output from other thermal generation including diesel generators, forcing emission higher in the short to medium-term.

Even if emissions were forced lower by premature withdrawal of Delta from the market it would likely lead to significant price escalation and a high potential of power shortfalls and in doing so be inconsistent with the price and reliability aspects of the NEO. The NEO must be views as a whole with all elements balanced to deliver in the long-term interests of consumers.

Please feel free to contact the EUAA if you have further questions.

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