esaa
Energy Supply Association of Australia www.esaa.com.au
ABN 98 052 416 083
Level 2
451 Little Bourke St
Melbourne
GPO Box 1823
Melbourne
Victoria 3001
P +61 3 9205 3100
F +61 3 9670 1069
E info@esaa.com.au

18 February 2013

Manager
Financial Markets Unit
Corporations and Capital Markets Division
The Treasury
Langton Crescent
PARKES ACT 2600

Lodged (by email): financialmarkets@treasury.gov.au

**Implementation of Australia's G-20 over-the-counter derivatives commitments – Proposals Paper**

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Commonwealth Treasury on the Implementation of Australia's G-20 over-the-counter derivatives commitments.

The esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of 36 electricity and downstream natural gas businesses. These businesses own and operate some $120 billion in assets, employ more than 51,000 people and contribute $16.5 billion directly to the nation's Gross Domestic Product.

The electricity derivatives market is local to Australia and is dominated by physical participants. Unlike some other derivatives markets, the electricity derivative markets are used to manage risk associated with physical positions, rather than speculate on future movements. Generators and retailers manage their exposure to the wholesale spot price of the NEM by entering into contractual arrangements that operate independently of both the wholesale spot market and the AEMO. Market participants can contract through the over-the-counter (OTC) and exchange (standardised) markets.

Even if only mandatory reporting was applied to electricity derivatives, it could result in a substantial cost to the electricity industry for little benefit. Electricity market participants would lose flexibility in hedging arrangements as some OTCs will become unavailable, resulting in less forward contracting. ACIL Tasman modelling commissioned by esaa found that if contracting was reduced by 5 per cent, it could result in retail electricity prices increasing by up to 10% for small-users and 15 per cent for large users.

Treasury is seeking feedback on the draft regulation requiring the Australian Security and Investment Commission (ASIC) to consult the Australian Energy Market Commission (AEMC) on derivative transaction rules. If after consultation with the Minister for Energy, the Minister for Financial Services deems it necessary to impose reporting requirements on electricity derivatives, esaa supports ASIC consulting the

AEMC prior to making a derivative transaction rule. We believe consultation is necessary given the AEMC's expertise and general understanding of the operation of the electricity market.

While we support the principle behind the draft regulation, we have a concern with the current wording. The second element of the requirement to consult "if the rule is about a matter connected with the Commission's functions" could create confusion. The AEMC is the rule making body for the NEM and also conducts reviews into the operation of various elements of the market, but is not involved in the day to day operation of the National Electricity Market. As such, there is a risk that "connected to Commission's function" may be interpreted too narrowly, limiting the circumstances in which consultation is sought. In our view ASIC should be obligated to consult the AEMC on any proposed derivative transaction rule that would have an impact on the electricity OTC market and it should be left to the AEMC to determine if they are able to provide any useful input.

esaa notes the Government will consider whether it is appropriate to impose mandatory requirements in relation to electricity derivatives after the AEMC's financial resilience review has been completed. We are comfortable with this approach. We would note that in their Issues Paper for the review the AEMC stated the "NEM financial markets are generally robust and have been able to evolve to accommodate major events and changes in market circumstances"[1].

Any questions about our submission should be addressed to Fergus Pope, by email to fergus.pope@esaa.com.au or by telephone on (03) 9205 3107.

Yours sincerely

**Kieran Donoghue**
General Manager Policy

[1] AEMC - NEM financial market resilience – Issues paper: http://www.aemc.gov.au/Media/docs/Issues-Paper-d67a2f10-7cb5-445b-9815-99880c37ac45-0.pdf