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Mr Percy Bell
Financial Markets Unit
Corporations and Capital Markets Division
The Treasury
Langton Crescent
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By email: financial markets@treasury.gov.au

Dear Mr Bell,

Implementation of Australia's G-20 over-the-counter derivatives commitments

EnergyAustralia welcomes the opportunity to comment on the Australian Treasury's 'Implementation of Australia's G-20 over-the-counter derivatives (OTC) commitments proposal paper' (the proposal paper).

EnergyAustralia is one of Australia's largest energy companies providing gas and electricity to over 2.7 million household customers. We own and operate an integrated portfolio of energy generation and storage facilities across Australia. We employ a range strategies to provide efficient solutions for our customers and effectively manage exposure to electricity spot market risk, including the use of OTC and exchange traded electricity derivatives.

We welcome confirmation in the proposal paper that no decisions will be made in respect to electricity derivatives until after completion of the Australian Energy Market Commission's national electricity market (NEM) financial market resilience review. It is important that the use, risks and benefits of electricity derivatives is considered within the overall context of Australia's highly regulated electricity market.

Electricity derivatives are primarily used by electricity market participants (generators and retailers) to manage risks associated with physical positions. The regulatory design of the mandatory energy only gross pool precludes direct physical contracting between generators and retailers. Generators must sell all output into the pool at the spot price and retailers must purchase from the pool. A comprehensive prudential regime is in place to manage the credit risk associated with the operation of this spot market.

Efficient operation of a gross pool market relies on the use of financial contracts to reduce volatility, manage participant risk and provide appropriate investment signals. In many cases electricity derivative contracts essentially replicate the physical contracts to supply electricity that would occur under alternate market designs (such as net pools). Any significant regulatory intervention in the electricity financial markets that is not coordinated with the overall regulatory design and structure of the market is likely to have unintended and potentially perverse consequences. Any such regulatory action that reduces the overall level of contract cover is likely to significantly increase electricity prices for consumers.

We support the draft regulation in the proposal paper to require ASIC to consult with the AEMC before making any derivative transaction rule relating to an electricity derivative, although we assume this would occur in any event as matter of good regulatory practice.

Section 7.5A.50(2) of the draft regulation would be simpler and clearer if it was shortened to read: '*ASIC must consult with the Australian Energy Market Commission before making a derivative transaction rule relating to an electricity derivative*'. It is not clear what the addition of the phrase '*if the rule is about a matter connected with the Commission's functions*' is intended to mean, this should be clarified or deleted.

We anticipate that the other questions in the proposal paper are best answered in respect to electricity derivatives within the context of the wider review of electricity financial markets referred to above.

Yours sincerely

Signed for email

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