

Case study: Origin Energy cost recovery claims under the RoLR framework 2024

1. Background

In 2022, a series of retailer failures triggered six Retailer of Last Resort (RoLR) events across the National Electricity Market between May 2022 and September 2022. Origin Energy Electricity Limited (Origin) was appointed as the designated RoLR and took on approximately 12,749 transferred customers.

Between February and June 2023, Origin submitted cost recovery applications seeking to recover \$4.33 million (after revisions) associated with supplying these customers. The applications represented the first time the Australian Energy Regulator (AER) had assessed cost recovery claims arising from actual RoLR events, requiring the AER to apply the legislative framework in a novel and complex setting.

The AER was required to determine whether Origin's claimed costs were recoverable under the National Energy Retail Law (Retail Law). In doing so, the AER was guided by 3 principles:

- the RoLR should have a reasonable opportunity to recover reasonable costs incurred
- cost recovery should allow for a return commensurate with risk
- the RoLR should bear a proportion of its costs.¹

A key feature of Origin's applications was that most cost categories were based on estimated methodologies rather than actual cost data. This required the AER to assess not only the quantum of costs, but also whether the methodologies used were reasonable and supported by evidence demonstrating a logical connection to the costs claimed.

The full determination on the cost recovery application process is available on the AER website: [Origin Retailer of Last Resort Cost Recovery Applications – Determination](#)

2. Assessment of evidence provided

Origin supported its applications with detailed spreadsheets, descriptions of its methodologies, and responses to requests for further information.

However, the AER noted that Origin relied heavily on portfolio-based estimates and was not able to provide detailed transactional evidence linking specific decisions or actions to the costs claimed.

The AER accepted that, under the framework, estimates may be used where actual costs are impractical to provide. This placed greater importance on the clarity of the methodology and the extent to which supporting material demonstrated a clear nexus between assumptions and the claimed costs.

¹ Since Origin's cost recovery applications were assessed, s 166(7)(c) of the Retail Law has been amended to replace the principle "the RoLR should bear a proportion of its costs" with "costs not prudently incurred by the registered RoLR in meeting its obligations should not be recoverable".

2.1 Revenue

Origin estimated revenue using Default Market Offer benchmarks and average consumption profiles rather than actual billing data. The AER accepted this approach, noting that Origin had provided reasonable explanations for the absence of actual data, including billing complexities and system migration, and that the resulting estimates were broadly consistent with DMO benchmarks.

2.2 Wholesale costs

Wholesale costs were the largest component of the claim. The AER assessed from both a direct cost and opportunity cost perspective.

The AER did not accept Origin's claim for direct wholesale costs. Origin had not provided evidence that it incurred additional costs in purchasing hedges or managing risk in response to the RoLR events. Origin confirmed that the increase in load did not trigger any specific hedging activity and did not result in breaches of its risk management thresholds. On this basis, the AER was not satisfied that direct costs had been incurred.

In contrast, the AER accepted that opportunity costs arose. The AER considered Origin's use of its generation portfolio to manage the additional load could have constrained its ability to sell hedges or earn spot market revenue. The AER accepted that this foregone revenue represented an opportunity cost and found that Origin's market-based methodology provided a reasonable proxy for quantifying that cost, despite being based on estimates.

2.3 Environmental costs

The AER accepted Origin's claim for direct environmental costs. It was satisfied that Origin would have been required to purchase additional renewable energy certificates to meet obligations associated with the transferred customers and that the methodology used to estimate these costs was reasonable and supported by market data.

However, the AER did not accept any claim for opportunity costs in relation to environmental certificates. As Origin is a net purchaser of certificates, the AER considered it unlikely that Origin forewent opportunities to sell certificates, and therefore no opportunity cost arose in this category.

2.4 Network costs

Network costs were estimated using DMO consumption profiles. The AER accepted this approach, noting that Origin was not seeking to recover amounts beyond what it had already recovered through customer revenue. The methodology was considered clear, logical and consistent with the treatment of network costs within the broader cost recovery framework.

2.5 Administrative costs

Origin initially included claims for labour costs for data analysts, business analysts and leadership costs, but removed those cost claims following AER enquiries into evidence to demonstrate the specific time it had devoted to each activity outside of business-as-usual activities. The remaining claim, consisting of estimated labour costs and actual postage costs, was accepted. The AER considered the reduced claim to be reasonable and appropriately supported by available evidence.

2.6 Costs to be borne by the RoLR

Origin proposed that it bear a portion of costs based on a customer acquisition cost benchmark. The AER accepted this approach, finding that it provided a transparent and reasonable method for allocating costs to be borne by Origin and that Origin demonstrated a clear relationship between the costs and the number of customers acquired.

As noted in Section 1 of this case study, the Retail Law has been amended and this objective is no longer applicable.

3. Cost recovery determination

The AER determined that Origin's applications reasonably established total recoverable costs and approved a net cost recovery amount of \$4.33 million. These costs were recovered from the relevant distributors (Endeavour Energy, Energex, Ergon Energy, Essential Energy and SA Power Networks) and spread evenly across their customer bases, resulting in an estimated one-off impact of approximately \$0.94 per customer.

Key insights from Origin RoLR cost recovery determination

Present a clear and coherent explanation of the claim

- Applications should present a structured explanation linking the RoLR event, the actions taken and the costs claimed during the specific circumstances. Applicants should note that completeness and clarity make it easier for the AER to progress the assessment efficiently.

Provide verifiable evidence to demonstrate costs incurred

- Applications should include supporting information that demonstrates costs were incurred and are attributable to the RoLR event.
- Claims for direct costs should reflect actions taken, supported by verifiable information. Records should include steps and the specific circumstances during which a decision was made. This should be documented along the process and provided as part of the cost recovery application.
- Applications should provide sufficient information to enable the AER to assess the reasonableness of cost claims, particularly for larger or more complex categories.

Provide clear and well-evidenced methodologies

- Where estimates are used, applicants should clearly explain methodology including assumptions, data sources and calculations.
- The methodology should demonstrate a reasonable basis for estimating costs.
- Opportunity costs should demonstrate genuine foregone revenue or constrained alternatives.
- Where genuine opportunity costs are claimed, applicants should explain how the RoLR event constrained commercial activities.
- The methodology should demonstrate a clear relationship between the event and the claimed foregone opportunity.

Ensure alignment between methodology and business practices

- Methodologies should be consistent with how the business manages risk and costs in practice.
- Claims should be consistent with the entity's documented processes and the actions taken during the RoLR event.
- Use reasonable proxies where direct measurement is not feasible, such as proxy or benchmark approaches to provide a logical and transparent basis for estimating costs.

Be prepared to refine claims where necessary

- Applicants may need to revise or remove elements of a claim where supporting information is insufficient. Updated information should be provided in a timely manner to ensure the AER can continue to progress assessment of the claim.