

25 August 2011

Sarah McDowell
Australian Energy Regulator
PO Box 520
Melbourne VIC 3001

By email: AERInquiry@ aer.gov.au



Re: AER Draft Retailer of Last Resort (RoLR) Package (July 2011)

Dear Sarah,

Envestra has reviewed the draft Retailer of Last Resort (**RoLR**) package released by the Australian Energy Regulator (**AER**) comprising the Notice of Draft Instrument and Draft Guidelines, Plan and Statement of Approach.

Envestra is generally supportive of the AER's approach regarding RoLR however detailed commentary has been made on the attached pages.

If you wish to discuss any of these matters further please contact me on (08) 8418 1128.

Yours sincerely

Ralph Mignone
Manager, Engineering and Technical Regulation

**Retailer of Last Resort (RoLR) Package
July 2011**

**Submission to
Australian Energy Regulator (AER)**

Approach

Following the AER's consultation on the RoLR scheme in December 2010, Envestra notes that in this second round, the AER has deviated little from its positions on issues which were of most importance to Envestra, namely cost recovery for distributors.

Envestra has therefore turned its attention to other general matters and matters within the RoLR Plan and Statement of Approach which are addressed below.

General Matters

1. Cost

One of the purposes of a ROLR scheme is to ensure continuity of supply to customers in the event of their retailer failing. It is important to recognise that in the event of a gas retailer failing (as opposed to an electricity retailer failing), there is less likely to be any discontinuity of supply to consumers, due to the nature of the commodity, i.e. it is a stored fuel and unlike electricity is not purchased half-hourly.

Gas distributors and their respective jurisdictions have therefore been at odds with the need for a RoLR scheme because whilst there are benefits of having automated systems ready in the background to cater for the rare incidence of a retailer failure, such systems come at exorbitant cost. A further inherent dilemma with ROLR systems is that their benefit increases in line with cost, akin to insurance.

Envestra acknowledges that industry is well beyond legislating the RoLR scheme out of the NECF; however ask that the AER bear in mind the costs on distributors to prepare for a RoLR event. Furthermore Envestra recommends that the AER's arrangements for a RoLR scheme generally aim to minimise overall costs to the industry to ensure that expenditure is prudent.

2. Timing & Implementation

Additional to the costs associated in preparing for a RoLR scheme, the AER should also be aware of the time required to implement the scheme when making regulatory arrangements; again for reasons of efficiency and prudence, but also in context of distributor readiness for compliance.



In order to implement industry-wide system changes for RoLR Envestra anticipates, given past experience; that the following steps are required:

- (i) Agreement on Retail Market Procedures via industry consultative committees
- (ii) Scoping of IT system changes to conform to updated Retail Market Procedures, to allow cost estimates and schedule development
- (iii) Board submission and funding approval in parallel with implementation of cost recovery arrangements
- (iv) Vendor selection and system change design
- (v) System change implementation
- (vi) User application testing / industry testing

Envestra further anticipates that these steps can take up to two years to implement, depending on scope i.e. whether industry is preparing for a Tier 1 or Tier 2 retail failure and the sophistication of the system changes i.e. fully automated or manual solutions.

The AER should therefore be aware of the transition required to move towards full compliance with the RoLR scheme, especially in the rare chance that a RoLR event occurs whilst distributors are making preparations.

Draft RoLR Plan

Sufficiency to cover all retail failures

As stated by the AER, the purpose of the RoLR Plan ("the Plan") is to set out the procedures to be followed by participants in a RoLR event, including direct communication with the customers of the failed retailer.

Envestra generally supports the Plan as drafted, however are concerned that it would fall short in the event of a tier 1 retail failure event. The sheer magnitude of transferring hundreds of thousands of customers from a failed tier 1 retailer to designated and/or additional RoLR's is not a straight forward process and designated and/or additional RoLR's may not have the capacity, function and contractual rights to gas and pipeline capacity or the financial and human resources to handle such an event.

Furthermore tier 1 retailer business are perhaps more likely to enter into Voluntary Administration before a RoLR event is triggered which would demand other procedures and processes.

Notification to the AER

Envestra also notes that section 2.6(b) of the Plan regarding information flows after a RoLR event is only applicable to electricity distributors. The section states that "an electricity distributor" will inform the AER when it has provided in accordance with the RoLR procedures, details of the failed retailer's customers to the designated RoLR's." Envestra interprets this to mean that gas distributors do not have the same obligation.



Draft RoLR Statement of Approach

2. Objectives of a RoLR Scheme

Envestra supports the AER's primary objectives for the national RoLR scheme which include:

- ❖ that customers maintain continuity of supply in the event of retailer failure; and
- ❖ that customers' interests are protected with respect to price (i.e. through competition in the RoLR appointment process) and other terms and conditions; and
- ❖ the integrity of wholesale market arrangements (i.e. payments between retailers and generators/upstream suppliers); and
- ❖ the continuity of payments to suppliers of transmission/distribution services and other ancillary energy service providers; and
- ❖ that RoLR's have an opportunity to recover reasonable costs.

Of particular importance to Envestra is the continuity of payments for distribution services.

➤ Continuity of Payments for Distribution Services

In the event of a retail failure, distributors prefer "business as usual" billing practices with the RoLR because this alleviates any significant and ongoing cash flow effects for distributors which would result from non-payment and it also provides certainty for credit risk.

Envestra acknowledges that Retail Support Rule 531¹ provides for cost recovery of unpaid distribution service charges where continuity of payments is not achieved, however the timeframes associated with the pass through process are uncertain for distributors and the arbitrary wording of the rule at sub-section 3 is a concern.

Timing

Regarding timeframes, Rule 531(2) provides that a distributor can apply for approval to vary a reference tariff with the AER within 90 days of the failure event; however there is no corresponding timeframes for the AER's approval. Envestra presumes these will then fall within the timeframes approved in the applicable access arrangements. According to Envestra's most recent decision for South Australia and Queensland for the 2011-16 period, the AER must notify Envestra of its decision to approve or reject the proposed variations within 90 business days of receiving the application.² If the AER needs more time to investigate or the matter is deemed difficult to assess, the AER has discretion to use an extended period of time.³

¹ National Gas (Retail Support) Amendment Rules 2010 Rule 531.

² Envestra SA Access Arrangement July 2011 Section 4.6.2 – Cost Pass Through Event Variations.

³ Ibid.



Distributors may therefore not recover unpaid service amounts for 6 months or more, if at all, which has a significant impact on distributors. Furthermore the magnitude of the impact is also affected by the size of the failure; hence if a tier 1 retailer became insolvent, the ramifications for distributors, let alone the energy market, would be severe.

Drafting of the Rule

Envestra's second concern regarding recovery of unpaid services if continuity of payments is not achieved, is that the drafting of sub-section 3 of Rule 531 is inconsistent with the Rules' apparent intent. The Rule is titled "Pass through of unpaid distribution service charges" and sub-section 3 reads as follows:

"The distributor must propose, and the AER must determine, a retailer insolvency pass through amount that **reflects the increase in the costs of providing reference services** that the distributor has incurred and is likely to incur until the end of the applicable access arrangement period solely as a consequence of the retailer insolvency event."

Envestra is uncertain as to whether unpaid distribution service charges could in fact be the subject of a pass through because it is questionable whether such charges would increase Envestra's costs of providing reference services. Inevitably a pass through amount to recover unpaid charges would increase the amount charged for a reference service, however Envestra is unsure as to whether outstanding payments are a cost of providing these services.

Electricity Issue

Envestra further notes that the issue of uncertainty around cost recovery for unpaid service charges also affects electricity distributors per section 6.6.1 of the National Electricity (Retail Support) Amendment Rules 2010, whereby instead of being the costs to provide reference services, recovery is for the costs of providing 'direct control services.'

The issues above therefore highlight the importance of continuity of payments for distribution services and in their support for the AER's primary objectives, Envestra hopes they do indeed underpin a retail failure event.

