



Notice of draft instruments

**Retailer of Last Resort (RoLR) guidelines**

**RoLR plan**

**RoLR statement of approach**

July 2011

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Inquiries about the currency of these guidelines should be addressed to:

Australian Energy Regulator  
GPO Box 520  
Melbourne Vic 3001

Tel: (03) 9290 1444  
Fax: (03) 9290 1457  
Email: [AERInquiry@aer.gov.au](mailto:AERInquiry@aer.gov.au)

### **Amendment record**

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	<b>Version</b>	<b>Date</b>	<b>Pages</b>
	DRAFT (CONSULTATION PURPOSES ONLY)	July 2011	60

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## Shortened forms

ACCC	Australian Competition and Consumer Commission
AER	Australian Energy Regulator
AEMO	Australian Energy Market Operator
Backup RoLR	A registered RoLR who may be designated if a default RoLR fails
National Energy Customer Framework	The National Energy Retail Law, National Energy Retail Rules and National Energy Retail Regulations
Distributor	Distribution Network Service Provider
Electricity Law	National Electricity Law
Electricity Rules	National Electricity Rules
RoLR register EoI	Retailer of Last Resort register Expression of Interest
Gas Law	National Gas Law
Gas Rules	National Gas Rules
NEM	National Electricity Market
Retail Law	National Energy Retail Law
Retail Regulations	National Energy Retail Regulations
Retail Rules	National Energy Retail Rules
RoLR	Retailer of Last Resort
STTM	Short term trading market
TNI	Transmission node identifier

## Retail consultation procedure

This notice and the attached Draft AER Retailer of Last Resort Guidelines (RoLR guidelines) have been published in accordance with the retail consultation procedure set out in cl. 173 of the National Energy Retail Rules (Retail Rules). As part of this consultation, the AER has also released a Draft RoLR statement of approach (RoLR statement of approach) and a Draft RoLR plan (RoLR plan).

The AER invites comments on the attached draft RoLR guidelines, RoLR statement of approach and RoLR plan. Responses to this consultation will inform the development of the AER's final RoLR guidelines, RoLR statement of approach and RoLR plan.

This is the final stage of the AER's consultation on these instruments. As advised in the Ministerial Council on Energy's Standing Committee of Officials Bulletin No. 190 on 21 March 2011, all activities carried out by the AER prior to the commencement of the National Energy Customer Framework (such as consultation, making instruments and decision-making) will be supported by appropriate transitional provisions enacted by participating jurisdictions. This will ensure instruments and decisions developed from these consultation processes are recognised under the National Energy Retail Law (Retail Law) and Retail Rules and take effect on commencement of the National Energy Customer Framework.

**Written submissions on the draft RoLR guidelines, draft statement of approach and draft RoLR plan are invited by Friday, 19 August 2011.** Submissions can be sent electronically to: [AERInquiry@aer.gov.au](mailto:AERInquiry@aer.gov.au) with the title "Draft AER RoLR Framework – attn Sarah McDowell", or by mail to:

General Manager, Markets Branch  
Australian Energy Regulator  
GPO Box 520  
Melbourne VIC 3001

*Submissions provided by email do not need to be provided separately by mail.*

### PLEASE NOTE:

The AER prefers that all submissions be publicly available to facilitate an informed and transparent consultative process. Submissions will therefore be treated as public documents unless otherwise requested, and will be placed on the AER's website ([www.aer.gov.au](http://www.aer.gov.au)). Parties wishing to submit confidential information are asked to:

- clearly identify the information that is subject of the confidentiality claim
- provide a non-confidential version of the submission for publication, in addition to the confidential one.

The AER does not generally accept blanket claims for confidentiality over the entirety of the information provided, including where a blanket claim is made as part of an email (e.g. in a standard form footer). Such claims should not be made unless all information is truly regarded as confidential. The identified information should genuinely be of a confidential nature and not otherwise publicly available.

In addition to this, parties must identify the specific documents or relevant parts of those documents which contain confidential information. The AER does not accept documents or parts of documents which are redacted or 'blacked out'.

For further information regarding the AER's use and disclosure of information provided to it, please refer to the *ACCC–AER information policy: the collection, use and disclosure of information*, which is available on the AER website under 'Publications'.

# 1 Introduction

## 1.1 Background

In March 2011, legislation to create a new National Energy Customer Framework was passed. The National Energy Customer Framework, comprising the Retail Law, National Energy Retail Rules (Retail Rules) and National Energy Retail Regulations (Retail Regulations) was developed by the Ministerial Council on Energy (MCE) following extensive consultation. In December 2010, the MCE agreed that jurisdictions would work towards a common target date of 1 July 2012 for commencement of the National Energy Customer Framework.

The Retail Law makes provision for a national Retailer of Last Resort (RoLR) scheme to provide common arrangements across jurisdictions in case of retailer failure. Retailer failure under the Retail Law can be triggered in a number of ways, including suspension from wholesale energy markets by the Australian Energy Market Operator (AEMO). The RoLR scheme is principally designed to ensure that in the event of retailer failure, arrangements are in place to ensure that customers continue to receive electricity and/or gas supply.

The AER has a number of responsibilities under the RoLR scheme. It is responsible for the registration and appointment of RoLRs and the determination of a RoLR cost recovery scheme to allow for the recovery of RoLR scheme costs in accordance with the provisions of Part 6 of the Retail Law. It is also responsible for developing procedures to be followed by RoLR participants in the event of retailer failure.

## 1.2 AER RoLR framework

The manner in which the AER proposes to undertake these functions is set out in three separate documents which are attached to this notice—draft RoLR guidelines, draft RoLR statement of approach and draft RoLR plan.

### 1.2.1 RoLR guidelines

Section 135 of Retail Law states:

- (1) The AER must develop, make and maintain AER RoLR guidelines in accordance with the retail consultation procedure.
- (2) The guidelines must—
  - (a) specify the circumstances in which the appointment of more than one designated RoLR for a RoLR event may occur; and
  - (b) specify the manner of determining the allocation of the designated RoLRs to particular customers or classes of customers; and
  - (c) provide for any other matter that the AER considers necessary in the circumstances.
- (3) The guidelines may (without limitation) make different provision for the failure of large retailers, small retailers and retailers that are default RoLRs.

- (4) The manner of determining the allocation of designated RoLRs referred to in subsection (2) must involve the use of meter identifiers alone or the use of a combination of meter identifiers and other means acceptable to AEMO, and must be determined by the AER in consultation with AEMO.
- (5) The guidelines may (without limitation)—
  - (a) specify the form of and information to be included in a RoLR register EoI; and
  - (b) specify the form of and information to be included in an application for a RoLR cost recovery scheme; and
  - (c) provide for any other matter the AER considers necessary with respect to the RoLR scheme.
- (6) The AER may amend the guidelines in accordance with the retail consultation procedure.

Reflecting the retail consultation procedure, the AER has attached draft RoLR guidelines to this notice of draft instruments.

The AER has also prepared a draft RoLR statement of approach, which is a broader more holistic document than the RoLR guidelines. Although the two documents work together and should be read together, only the RoLR guidelines is the formal instrument under s.135 of the Retail Law.

### **1.2.2 RoLR statement of approach**

While not required under the Retail Law, the AER has also decided to set out a broader RoLR statement of approach. This is designed to complement the RoLR guidelines by providing other information on RoLR registration and appointment and RoLR cost recovery to assist industry understand the operation of the overall RoLR framework.

In particular, the draft RoLR statement of approach provides information on:

- when the AER will call for expressions of interest to register as a RoLR, and
- when the AER will make a “designation decision” (the decision to appoint someone as a RoLR) and if it does, what information it will use to make its decision.

The draft RoLR statement of approach also sets out general principles the AER will consider when making a cost recovery scheme determination. It sets out typical RoLR event scenarios and the proposed approach to cost recovery schemes for these scenarios. However, it should be noted that the AER is required to make a cost recovery scheme determination on a case by case basis for each retailer designated as a RoLR.

### **1.2.3 RoLR plan**

The Retail Law requires the AER to develop, make and maintain RoLR plans. The RoLR plan outlines:



- procedures to be followed by the participants in the event of a RoLR event, including direct communication with customers of a failed retailer; and
- procedures for conducting RoLR exercises which are to be carried out by participants in the plan.

The AER has set out in its draft RoLR statement of approach the proposed procedures to be followed by participants during a RoLR event and the proposed nature of the RoLR exercises.

### **1.3 Purpose of RoLR draft notice**

The purpose of this notice is to outline the AER's overall RoLR framework. To facilitate consideration of the entire suite of RoLR issues, the AER has decided to explain the RoLR guidelines, RoLR Statement of Approach and RoLR plan in this one document.

The draft notice is also designed to provide the AER's position on issues raised in submissions to the RoLR issues papers released by the AER in November 2010.

### **1.4 Structure of RoLR draft notice**

The RoLR draft notice is structured as follows:

- Chapter 2 sets out registration and appointments issues, which are covered in both the draft RoLR guidelines and the draft statement of approach. It also responds to submissions received in response to the AER's registration and appointments issues paper.
- Chapter 3 sets out RoLR cost recovery issues, which are covered in both the draft RoLR guidelines and the draft statement of approach. It also responds to submissions received in response to the AER's RoLR cost recovery issues paper.
- Chapter 4 sets out the RoLR plan and responds to issues received in response to the RoLR plan issues paper.

## 2 RoLR registration and appointment

This chapter discusses matters covered in both the RoLR guidelines and the RoLR statement of approach.

In respect of the RoLR guidelines, this chapter outlines the AER's draft decision on the form and information to be included in RoLR register Expressions of Interest (RoLR register EoIs). It also specifies the circumstances when more than one designated RoLR may be appointed and how they will be allocated to customers. These decisions form the registration and appointment content of the RoLR guidelines and are being consulted on in accordance with the requirements of Part 6 of the Retail Law.

In respect of the RoLR statement of approach, this chapter outlines the AER's intended approach on other issues important to the RoLR scheme registration and appointment framework (RoLR R&A framework) including:

- standing instructions to AEMO for default RoLR failures and for backup RoLR failures
- when the AER will call for expressions of interest
- the AER's registration process, including reviews of registrations
- the designation process, including timing aspects and
- the exercise of contingency event powers.

The AER considers that outlining its position on these issues in a draft statement of approach will assist retailers to understand the RoLR registration and appointment process.

### 2.1 Submissions received on the RoLR registration and appointment issues paper

In November 2010, the AER released a RoLR registration and appointments issues paper (RoLR appointment issues paper)<sup>1</sup>. In developing its draft decision on the RoLR guidelines and in preparing the draft RoLR statement of approach, the AER has considered the views expressed in the submissions received on the RoLR appointment issues paper.

The AER received submissions from the following parties:

- ActewAGL
- AEMO
- AGL

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<sup>1</sup> AER, *RoLR appointments issues paper*, November 2010, <http://www.aer.gov.au/content/index.phtml/itemId/741303>.

- Citipower and Powercor (Citipower/Powercor)
- Envestra
- Ergon Energy
- ETSA Utilities (ETSA)
- Jemena
- Origin Energy
- SP Ausnet
- United Energy Distribution and Multinet Gas (UED/Multinet).

The main issues raised were in relation to:

- the objectives of a RoLR scheme
- the AER's general approach to the registration framework
- default RoLR registration arrangements
- additional RoLR registration arrangements
- backup RoLR arrangements (where a default RoLR fails)
- the AER's general approach to the designation framework
- multiple RoLR appointments and
- the grouping of customers for designation.

## **2.2 Registration and appointment issues**

### **2.2.1 Objectives of the RoLR scheme**

The AER considers it important to set out the objectives it will use to develop its RoLR R&A framework. Therefore, in the RoLR appointments issues paper, the AER proposed a list of objectives to guide the RoLR registration and appointment process and sought comment. The AER has taken the National Energy Retail Objective (retail objective) as a starting point in specifying these objectives.<sup>2</sup>

AGL supported the objective of ensuring the continuity of wholesale market payments between industry participants so that the power stays on for consumers. The AER has retained this as a primary objective of the RoLR scheme.

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<sup>2</sup> The National Energy Retail Objective is set out in s. 13 of the National Energy Retail Law. It states the objective of the law is to promote the efficient investment in, and efficient operation and use of, energy services for the long term interests of consumers of energy with respect to price, quality, safety, reliability and security of supply of energy.

UED/Multinet proposed as a further primary objective the maintenance of the integrity and confidence in the whole market in a RoLR event. In its RoLR appointment issues paper, the AER listed the maintenance of the integrity of wholesale markets, the continuity of payment to other energy market participants and protection of customers' interests as primary objectives. The AER considers these objectives already adequately capture UED/Multinet's proposal.

Further, UED/Multinet proposed as a primary objective an approach that allows a simple RoLR process to be implemented quickly by all parties, including simple, effective communication with customers. The AER agrees with UED/Multinet that any RoLR scheme developed should be able to be administered quickly and simply. However, the AER does not believe it is necessary to list this principle as a primary objective as it is already captured by the reference to the protection of customers' interests in the scheme objectives.

#### **Draft RoLR statement of approach**

As proposed in section 3 of the draft RoLR statement of approach the AER considers the primary objectives for the national RoLR scheme are to ensure:

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

#### **2.2.2 General approach to the registration framework**

The AER must consider the RoLR criteria under s. 125(6) in respect of registering and appointing default RoLRs and s.126(2) in respect of registering additional RoLRs. This section of the notice considers the general approach to the registration of RoLRs. The following section focuses on default RoLR registration and appointment and then section 2.2.4 focuses on additional RoLR registration.

Under s. 135(5)(a), the AER may specify in RoLR guidelines the information to be included in a RoLR register EoI. However, the AER is not required to register a retailer as a RoLR even if it meets the RoLR criteria.<sup>3</sup> Section 127 of the Retail Law requires the AER to maintain and publish on its website a register of RoLRs.

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<sup>3</sup> s. 125(11), 126(9) National Energy Retail Law.

## **RoLR criteria**

In its November 2010 RoLR appointment issues paper, the AER sought comment on each of the RoLR criteria<sup>4</sup>:

- financial resources
- organisation and technical capacity
- suitability
- any other relevant matters specified in the energy laws
- other matters considered relevant in the circumstances.

### *Financial resources*

AGL, Citipower/Powercor, Envestra, and Origin Energy all identified financial resources as the key RoLR criterion. The AER agrees that this criterion is critical. RoLRs will need to be able to immediately meet requirements for increased wholesale market prudentials as a result of customer acquisition. If retailers don't have sufficient resources then cascading retailer failures may follow soon after the initial RoLR event. AEMO considered that the AER should have regard to the ability of retailers to procure bank guarantees at short notice when assessing the financial resources criterion. The AER agrees and will require information on the ability to procure additional bank guarantees when a retailer applies to be a RoLR.

Jemena also considered the AER should take account of how close the retailer is to existing credit limits in respect of distributor obligations. The AER agrees that it should require information as to the status of credit limits with distributors and the on-going ability to maintain these limits.

The AER has included a full list of the information it will require from applicants in relation to this criterion in its draft RoLR guidelines.

### *Organisational & technical capacity*

SP Ausnet emphasised the importance of RoLRs having the technical capacity to undertake RoLR responsibilities. The AER agrees it is important that RoLRs have the technical capacity to deal with matters such as the provision of data sets and proposes seeking information on this capability when retailers apply. For example, the Jackgreen RoLR event demonstrated the need for businesses to have capabilities to deal with data issues which inevitably arise at the time of RoLR events.

The AER has included a full list of the information it will require from applicants in relation to this criterion in its draft RoLR guidelines.

### *Suitability*

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<sup>4</sup> s.123(1) National Energy Retail Law.

UED/Multinet considered that where there is no declared wholesale gas market or Short Term Trading Market (STTM), the AER's defining criterion should be whether the retailer has the appropriate contractual arrangements to supply any transferred customers as opposed to using/relying on the AER's directions in the Retail Law. The AER agrees that it would be ideal that any default RoLR for these gas networks be able to demonstrate it has contractual arrangements to take on the transferred customers. Further, the AER will not register additional RoLRs against networks if they do not have contracts in place to ship gas.

The AER has included a full list of the information it will require from applicants in relation to this criterion in its draft RoLR guidelines.

#### *Other matters relevant in the circumstances*

As an extension of the financial resources criterion, the AER believes that it should consider in relation to large retailer failures, RoLR arrangements which lessen the risk of cascading retailer failures. This can be achieved by sharing the distribution of connection points / gas distribution systems at the time of a RoLR event between a number of registered RoLRs (as discussed at section 2.2.8 below). Having regard to the 'worst case scenario' of a large retailer failure, the AER will consider the need to appoint different retailers as default RoLRs for different areas, because a spread of different default RoLRs would be better able to absorb those customers without failing themselves.

#### **Other matters the AER will have regard to when registering RoLRs**

The Retail Law allows retailers to propose any condition when expressing an interest to be a registered RoLR and allows retailers to express interest at any time to be a RoLR.<sup>5</sup> However, as the AER noted in its RoLR appointment issues paper, a retailer is not automatically entitled to registration as a RoLR even though it satisfies or appears to satisfy the RoLR criteria.<sup>6</sup> The AER may choose not to register a retailer to be a default/additional RoLR even if it satisfies the RoLR criteria. This will enable the AER to:

- limit the nature of conditions which are allowed to be attached to a RoLR register EoI
- limit the timing of when RoLR register EoIs can be submitted and
- impose some limits on the grouping of connection points for RoLR registration.

The AER believes this is required to meet RoLR scheme objectives and promote a streamlined practical scheme. The AER considers different types of conditions in the following sections dealing with default RoLRs and additional RoLRs separately.

#### **RoLR register**

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<sup>5</sup> ss. 124(2), 124(5) National Energy Retail Law.

<sup>6</sup> ss. 126(9), 125(11) National Energy Retail Law.

Section 127 of the Retail Law requires the AER to maintain and publish a register of RoLRs on its website. The register of RoLRs must include particulars of the RoLRs registered, and must indicate whether the retailer is registered as a default RoLR or as an additional RoLR.

In the RoLR appointment issues paper, the AER asked stakeholders to identify any problems that may occur with the full disclosure of registration conditions. Further, the AER asked retailers whether the disclosure of information may influence a retailer's decision to seek additional RoLR registration.

Envestra and UED/Multinet supported the publication of registration information. In particular, Envestra considered that full publication of registration data will assist market participants flag potential issues that may arise as a result of a particular condition.

In contrast, Origin Energy argued that not all RoLR terms and conditions should be disclosed on the RoLR register. They stated that a term or condition, such as prudential limits, is of a commercial nature and its publication may discourage RoLR participation.

The AER does not want the RoLR register to expose retailers to any unnecessary commercial risk. Therefore, to prevent this from occurring, only the term or condition heading will be included in the RoLR register. This may include 'customer numbers' or 'customer load' but not detailed customer specifics such as the exact amount of customers a retailer is prepared to be designated. The AER notes that a term or condition can only be attached to the registration of a RoLR if the AER accepts it, having considered the RoLR criteria.

#### **Draft decision on RoLR guidelines**

As proposed at Appendix A of the draft RoLR guidelines, the AER has specified the information to be included in a RoLR register EoI to demonstrate a retailer meets the following RoLR criteria:

*Financial Resources*—the information the AER proposes requiring under this criterion includes information as to the ability to procure additional bank guarantees at the time of event and information as to the meeting of distributor network payment and market payment obligations.

*Organisational and technical capacity*

*Suitability*—the information the AER proposes requiring under this criterion includes information as to the ability to take on gas customers based on contractual arrangements with pipeline operators.

#### **Draft RoLR statement of approach**

As proposed at section 3 of the draft RoLR statement of approach the AER has specified its proposed approach to:

- calling for expressions of interest to be a registered RoLR
- registering RoLRs in accordance with the RoLR criteria
- reviewing RoLR registrations
- publication of RoLR register information and
- backup RoLR arrangements for default RoLR failures.

### **2.2.3 Default RoLR registration arrangements**

Subsection 125(2) of the Retail Law requires that there must be only one default gas RoLR registered to each distribution system and one default RoLR for each electricity connection point. For electricity there are options to group connection points for the purpose of registering default RoLRs (and additional RoLRs). For example, connection points and attendant national metering identifiers (NMIs) could be grouped by transmission node identifiers (TNIs), local retail areas, National Electricity Market (NEM) jurisdictions or postcodes. Having registered a default RoLR under s.125(9) of the Retail Law, the AER may then terminate the registration of a default RoLR at any time.

In its RoLR appointment issues paper the AER sought comment on:

- whether current jurisdictional RoLRs should be registered as default RoLRs initially
- the preferred registration basis for default RoLRs for electricity (i.e. should it be by TNI, local retail area, NEM jurisdiction or postcode)
- whether a three year review period for default RoLR registrations was appropriate and
- what circumstances or events should require the AER to review or terminate a default RoLR registration.

#### *Initial default RoLRs*

UED/Multinet, Ergon Energy and Origin Energy supported existing jurisdictional RoLRs being appointed as initial default RoLRs for a period of time. UED/Multinet noted an example of where there was presently no RoLR appointed in South Gippsland, Victoria. ETSA's submission highlighted that it does not want to be appointed the jurisdictional RoLR in South Australia, noting that at the moment it contracts out its RoLR role to a large retailer.

The AER notes that default RoLR arrangements are likely to be a matter for jurisdictions to consider within their transitional arrangements. However, it is likely that the AER will have to make some default appointments prior to the National Energy Customer Framework commencing, in particular where there is no existing default RoLR or where a distributor is the RoLR. The AER will consider what (if any)



further default RoLR arrangements are required once transitional arrangements have been finalised.

#### *Preferred grouping of electricity connection points for registration*

Ergon Energy and ETSA supported default RoLRs being registered to local retailer areas. Ergon Energy considered this would be easier to manage from an operational point of view whilst ETSA considered if default RoLRs were appointed based on TNIs this would increase the costs and complexities. AEMO stated that TNI and local retailer areas were workable registration methods based on its current systems and added that any other methods would require costly system changes for AEMO and also likely for participants. Origin Energy did not support a single default RoLR for a jurisdiction.

The AER notes that in the short term it is likely that existing retailers carrying out the RoLR role will become the default RoLRs within their jurisdictions. This may mean that some default RoLRs cover a whole jurisdiction (for example, potentially AGL in South Australia for electricity) or cover local retailer areas (e.g. NSW, Victoria).

As competition develops further in energy markets, retailers' customer bases are becoming less centred on traditional local areas. The AER considers that for default RoLR registration, the grouping of connection points by TNI, local retailer area or even NEM jurisdiction should be considered. When making registration decisions, the AER will give regard to default RoLR arrangements which ensure the integrity of the wholesale market. Default RoLR arrangements should lessen the risk of cascading retailer failures by, to the extent possible, sharing connection points between a number of default RoLRs. This approach will assist to limit the exposure of retailers to immediate increased wholesale market prudential requirements and increase the likelihood that the default RoLR will have sufficient financial resources at the time of a RoLR event. Therefore, the AER will consider whether TNIs (which consist of less connection points than local retailer areas or NEM jurisdictions) provide a better means of sharing load should a large retailer fail.

#### *Treatment of conditions for default RoLRs*

As noted in the November 2010 RoLR appointments issues paper, while all retailers applying for registration may express interest in being a RoLR subject to conditions under s. 124(4) of the Retail Law, the AER considers that it is not feasible for default RoLRs to propose conditions other than in relation to a cost recovery scheme. This is because default RoLRs will need to be able to acquire any number (or class) of customers for where they are registered. This approach is necessary to meet the RoLR scheme objective of ensuring that customers maintain continuity of supply by ensuring that there always exists one retailer responsible for all customers should a RoLR event occur. However, the AER does consider that default RoLRs should not be prohibited from proposing conditions relating to cost recovery. This may include default RoLRs proposing not to recover RoLR event costs to attain a competitive advantage over additional RoLRs.

#### *Periodic review of default RoLR registrations*

Origin Energy considered that default RoLR registrations should be reviewed at a minimum every three years whilst ETSA stated that it should be every three to five years to minimise costs. UED/Multinet considers default RoLR registrations should be an evergreen appointment subject to certain events.

The AER will review default RoLR arrangements every three years. Three years strikes a balance between allowing for default RoLR arrangements to be reconsidered holistically from time to time and allowing retailers to express interest in being a default RoLR, with, broader operational/administrative considerations. The operational costs of retailers, distributors and AEMO are likely to be less if default RoLRs are fixed for a period of time. The AER also notes that reviewing default RoLR arrangements will create an administrative burden on the AER / AEMO and any parties considered for registration and believes that this burden would be too great if arrangements were reviewed on a more regular basis.

#### *Ad-hoc expressions of interest*

The AER prefers that there not be RoLR register EoIs to be a default RoLR submitted outside the three yearly reviews. This is because of the operational and administrative considerations discussed above. However, the AER notes that following an event in the market it may call for RoLR register EoIs.

#### *Ad-hoc review of default RoLR arrangements*

Submissions by Origin Energy, UED/Multinet and Envestra noted the following events may require a review of default RoLR arrangements:

- mergers, changes in market share, change in business orientation
- issues with payments to distributors
- significant complaints/compliance issues and
- market system changes.

The AER agrees it may review the RoLR arrangements following these events as there may be a material change to a retailer or the market affecting the ability of retailer(s) to act as default RoLRs. The AER will monitor the occurrence of these events.

#### **Draft decision on RoLR guidelines**

As proposed at Appendix A of the draft RoLR guidelines the AER has set out a form for RoLR register EoI to be a default RoLR.

#### **Draft RoLR statement of approach**

As proposed at section 3.3 of the draft RoLR statement of approach the AER has set out:

- RoLR criteria requirements—For default RoLRs the AER proposes not accepting any conditions attached to RoLR register EoIs to limit the number of customers or customer load to be transferred at the time of a RoLR event.
- Periodic review and ad-hoc reviews of default RoLRs—The AER proposes reviewing default RoLR arrangements every three years. The AER will review default RoLR arrangements outside the three year review periods wherever the AER identifies there has been a material change to a retailer or the market affecting a retailer(s) ability to act as a default RoLR.
- Expressions of interest for default RoLRs—The AER proposes calling for RoLR register EoIs 6 months before the end of each three year period, or in shorter time frames should, for example, a default RoLR exits the market suddenly.

As proposed at s 3.5 of the draft RoLR statement of approach the AER has set out:

- Preferred grouping of electricity connection points for registration—After transitional arrangements, the AER may choose to register default RoLRs against TNI, Local retailer area or NEM jurisdiction (for electricity) having had regard to any RoLR register EoIs, the RoLR criteria and the RoLR scheme objectives.

## **2.2.4 Additional RoLR framework**

Under s. 126 of the Retail Law, the AER may register one or more retailers as an additional RoLR for a connection point (in electricity) or a distribution system (in gas). The AER may also impose conditions on the retailer’s registration as an additional RoLR with the retailer’s consent.

In the November 2010 RoLR appointments issues paper, the AER proposed two categories of additional RoLR registration—a firm offer category and non-firm offer category. It proposed standard terms and conditions to be attached to an additional RoLR with firm offer registration. It also proposed preferred geographic areas for registration and potential registration review arrangements. This section recaps on these issues, summarises stakeholder views and outlines the AER’s proposed approach on these arrangements.

### *Categories and timeframes of additional RoLRs*

The AER set out in the issues paper two potential categories—additional RoLR with firm offer and additional RoLR with non-firm offer.

The additional RoLR with firm offer category commits a retailer to being a designated RoLR, if required by the AER. The additional RoLR with firm offer will be able to impose conditions upon its appointment of designated RoLRs, including establishing the number and class of customers it is prepared to take on. Registration as an additional RoLR with firm offer will be valid for three months. At the end of the three months, the AER will ask the retailer to confirm whether there have been any material changes to the information provided in the business’ RoLR register EoI.

The additional RoLR with non-firm offer category enables retailers to register their interest to act as a designated RoLR. The additional RoLR with non-firm offer will

not be appointed by the AER unless they indicate their interest to the AER at the time of the RoLR event. Registration as an additional RoLR with non-firm offer will be valid for two years. At the end of this period, the AER will review the registration of the retailer as an additional RoLR with non-firm offer.

Origin Energy supported the two categories of additional RoLR registration proposed by the AER. It suggested any further categories will most likely be variations on the two broad categories already identified. The AER has decided to include in the draft RoLR guidelines the two forms of additional RoLR registration outlined in the issues paper, a firm offer category and non-firm offer category. The AER considers by providing for these two categories of additional RoLR registration, the likelihood of non-default RoLRs acting as a designated RoLR is increased. This may potentially achieve consumer benefits, such as no RoLR cost recovery, while not compromising customers' supply in a RoLR event.

#### *Areas of registration*

Under s. 126 (1) of the Retail Law, the AER may register additional RoLRs for each connection point in electricity and for each distribution system in gas.

In the RoLR appointment issues paper, the AER proposed different ways retailers may register as additional RoLRs for electricity connection points, including by NEM jurisdiction, TNI or local retailer area. The AER suggests by registering retailers per NEM jurisdiction, retailers will have a greater chance of acting as the designated RoLR for a RoLR event. Registration by jurisdiction also provides the AER with the flexibility to decide how it may designate multiple RoLRs to different TNIs during a RoLR event.

Origin Energy argued that while registration on the basis of TNI may provide flexibility, it may also increase complexity within the RoLR scheme. Origin Energy considered if the AER consults on TNI registration, its scope must include its implications for event management costs.

The AER agrees that registering additional RoLRs on the basis of TNI will create complexity and limit the ability of retailers to act as the designated RoLR. The AER is therefore proposing that additional RoLRs in electricity register on the basis of jurisdiction. Gas retailers will register as an additional RoLR on the basis of a gas distribution system.<sup>7</sup>

#### *Terms and conditions*

Under s. 124(4) of the Retail Law, retailers may propose conditions under which they are prepared to be appointed when they apply for RoLR registration. The AER may also impose conditions on the registration of an additional RoLR with the retailer's consent.<sup>8</sup>

The Retail Law allows a retailer to propose conditions on the number or class of customers it accepts as a designated RoLR. Further, it enables a retailer to propose

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<sup>7</sup> s.126(1) National Energy Retail Law.

<sup>8</sup> s.126(7) National Energy Retail Law.

variations to its RoLR cost recovery scheme. For example, the retailer may propose to waive RoLR event costs altogether.

The issues paper proposed other conditions for additional RoLRs, including prudential limits and market price. Under the condition of prudential limits, the retailer may agree to take on a certain number of customers on the basis it will not cause the retailer to exceed its credit limits. For market price, retailers may specify the wholesale energy market conditions under which they would be prepared to be designated as an additional RoLR. By providing this condition, the potential for cascading failure may be reduced.

Envestra and Origin Energy generally supported the AER's approach to establishing RoLR terms and conditions. In particular, Envestra agreed with the AER providing for additional RoLR terms and conditions which may limit or mitigate the risk of cascading failure.

Origin Energy considered the terms and conditions of additional RoLRs should be streamlined at an early stage. Origin Energy noted retailers will be able to propose additional terms and conditions, but will do so cognisant this may lead to them not being appointed as the RoLR.

The AER proposes to enable retailers applying for additional RoLR registration to establish certain prudential or wholesale price limits. However, the AER considers these conditions are only appropriate to retailers seeking to register as an additional RoLR with firm offer. Additional RoLRs with non-firm offers have the ability to assess their prudentials or wholesale market conditions before expressing interest to be the designated RoLR for a RoLR event.

The AER, however, agrees with Origin Energy that the terms and conditions for additional RoLR registration should be streamlined. Therefore, while the AER will enable prudential or wholesale price limits to be proposed by additional RoLRs in the firm offer category, they will not constitute the 'base' terms and conditions set out in the RoLR register EoI documentation.

The AER is proposing six terms and conditions to be included in the RoLR register EoI documentation (which can then be supplemented to enable prudential or wholesale price limits), including:

- Jurisdiction/ Distribution system—Electricity retailers will be able to identify which jurisdiction/s they are prepared to serve as the designated RoLR. Gas retailers will be able to nominate the distribution system/s for which they are prepared to act as the designated RoLR.
- Customer numbers—Retailers may identify the number of customers they are prepared to serve as the designated RoLR.
- Customer class—Electricity retailers may identify whether they are prepared to serve large or small customers as the designated RoLR. Designated RoLRs in gas will be required to take on all customer classes, since only one registered RoLR may be appointed as the designated RoLR for a gas distribution system under the Retail Law.

- Customer load—Retailers may nominate the customer load they are prepared to take on as the designated RoLR.
- Cost recovery variation—Retailers may nominate how they intend to vary their RoLR cost recovery scheme, such as waiving RoLR event costs.
- No consultation before appointment (for additional RoLRs with firm offers)—Retailers agree to be appointed as a RoLR without first being consulted by the AER.

These categories limit the exposure of additional retailers during a RoLR event, particularly additional RoLRs with firm offers. They also establish a streamlined framework which provides enough information and flexibility to the AER to assign customers to additional RoLRs.

In relation to customer class, the AER acknowledges there are differences between electricity jurisdictional consumption thresholds and the thresholds proposed in the National Energy Retail Regulations. For electricity AEMO's systems currently reflect consumption thresholds based on jurisdictional metrology thresholds. This may produce a disconnect between the NECF classification of small/large customers and the classifications able to be used by AEMO for the purpose of RoLR transfers if different classification levels of small and large apply. The AER will need to consider whether usage of NMI classifications (only present system available) of small/large customers will create any issues with the protection of small/large customers under the broader RoLR framework.

#### *Expressions of interest*

The AER is proposing to seek and consider RoLR register EoIs to be an additional RoLR every 12 months. The AER considers the 12 month interval provides a balance between encouraging new retailers to register as an additional RoLR and maintaining an efficient and streamlined RoLR administrative framework. The AER prefers that retailers do not apply to be an additional RoLR outside this period.

#### *Periodic review of additional RoLR arrangements*

The issues paper proposed that the AER will review the registration of additional RoLR with firm offers every 3 months and for an additional RoLR with non-firm offer every 2 years.

Origin Energy agreed with the AER that the registration of an additional RoLR with firm offer should be for a limited period. Origin Energy noted that experience over time will assist the AER and industry in determining the appropriate interval.

The AER agrees with Origin Energy that over time the AER may need to reassess the interval within which additional RoLR registration is reviewed. However as a starting point, the AER is continuing to propose that it reviews the registration of additional RoLRs with firm offers every three months and for additional RoLRs with non-firm offer, every two years.

#### *Ad hoc review of additional RoLR arrangements*

The AER noted in the issues paper that it would review the registration of a default RoLR, if there were material changes to the retailer. However, it did not comment on whether the AER would undertake ad hoc reviews of additional RoLRs.

The AER considers it is appropriate to undertake an ad hoc review of an additional RoLR if it appears they no longer satisfy the RoLR criteria. Similar to ad hoc review arrangements for default RoLRs and backup RoLRs, the AER would consider reviewing the registration of an additional RoLR if it had systemic breaches or a call notice/margin call issued against it.

#### **Draft decision on RoLR guidelines**

As proposed at Appendix B of the draft RoLR guidelines:

- Categories—the AER proposes two forms of additional RoLR registration in the additional RoLR EoI being a firm offer category and non-firm offer category.
- Terms and conditions—the AER proposes six standard terms and conditions, including jurisdiction, customer numbers, customer class, customer load, cost recovery variation and for firm offers only, a condition whereby retailers agree to appointment without being consulted. Other terms or conditions may also be proposed by the AER or retailer.

#### **Draft RoLR statement of approach**

As proposed at section 3.4 of the draft RoLR statement of approach:

- Expressions of interest—the AER proposes to seek and consider EoIs to be an additional RoLR every 12 months.
- Periodic review of additional RoLR registration—the AER proposes to review the registration of additional RoLRs (with firm offers) every three months and for additional RoLRs (with non-firm offer) every two years.
- Ad hoc review of additional RoLR registration—the AER proposes to undertake an ad hoc review of an additional RoLR if it appears they no longer satisfy the RoLR criteria.

As proposed at section 3.5 of the draft RoLR statement of approach:

- Area of registration—the AER proposes that additional RoLRs in electricity register on the basis of jurisdiction. Gas retailers seeking to register as an additional RoLR must register on the basis of gas distribution system.

### **2.2.5 Backup RoLR arrangements**

For the RoLR scheme to deal with the failure of any retailer it must provide for RoLR arrangements which encompass a default RoLR itself failing. The Retail Law does not make specific provision for default RoLR failures, other than noting that the AER may make provision for default RoLR failures as part of its RoLR guidelines.

In the RoLR appointments issues paper the AER noted that the Victorian arrangements could be used as a template, but acknowledged that other jurisdictions might require different arrangements.

Envestra supported the AER's proposal to develop backup arrangements for other jurisdictions using Victoria's arrangements as a template, while allowing for any differences in jurisdictional needs. UED/Multinet supported the concept of allocating customers (on the basis of TNI) to two RoLRs for a local retailer area, should a local retailer fail. For gas, the businesses supported the appointment of the other local retailers as the designated RoLRs in the event of a local retailer failure. The AER agrees with these submissions noting they reflect the current Victorian approach. This approach is to transfer customers to, and in the case of electricity to split customers between, remaining large retailers in the case of default RoLR failures. This approach uses grouping mechanisms supported by AEMO/distributor systems—TNIs for electricity and distribution systems for gas.

UED/Multinet noted that if one of the three Victorian incumbents failed (AGL, Origin Energy, or TRUenergy) that this would be a significant failure across electricity and gas which may require government intervention. They noted also that these incumbents may have significant obligations interstate.

Origin Energy considered the AER should enhance the current Victorian approach by allowing additional RoLRs with firm offers to participate when default RoLRs fail. Where the AER has time to consider additional RoLR offers before a RoLR event, it will consider splitting affected customers between additional RoLRs and default RoLRs if it considers this is appropriate having considered the designation criteria. It may for example appoint an additional RoLR to be the designated RoLR if it considers this will lessen the possibility of cascading retailer failures by reducing the amount of customers designated to remaining default RoLRs.

Further, the AER agrees with Origin Energy's comments that it should consider firm additional RoLR offers for inclusion in standing instructions to AEMO as a backup to RoLR arrangements. The AER will finalise initial standing instructions to AEMO once registered default RoLRs and additional RoLR offers are known.

Under backup RoLR arrangements the AER may need to appoint registered RoLRs to be the designated RoLR for connection points they are not registered against.<sup>9</sup> In fact, this is the only practical way backup RoLR arrangements could work at the time of a RoLR event given only one default RoLR can be registered against each connection point. For example, if default RoLR X is registered as a RoLR for one area of customers; the AER will need to appoint default/additional RoLRs to be the designated RoLRs from other areas should retailer X itself fail. Accordingly, the AER will need to consider whether a RoLR registered in one jurisdiction is a suitable retailer to retail energy to customers in another jurisdiction.

The AER notes that following recent retailer acquisitions the initial default RoLRs across many jurisdictions are likely to be TRUenergy, AGL and Origin Energy.

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<sup>9</sup> s. 132(2) of the National Energy Retail Law allows the AER to do this.



Therefore, backup arrangements for a failure of these three retailers would potentially involve the redistribution of millions of customers.

#### *Grouping of connection points for backup RoLR arrangements*

As highlighted above, submissions supported splitting up customers under backup RoLR arrangements on the basis of TNI for electricity and distribution systems for gas. In jurisdictions where it is viable, the AER will seek to split customers on this basis.

The AER's approach to providing for backup RoLRs will be to group default RoLR customer connection points for that default RoLR area consistent with the RoLR scheme aims and objectives, notably maintaining the integrity of wholesale markets and the continuity of payments at the time of a RoLR event. For this purpose, the AER will likely use the smallest of these grouping of connection points, TNIs, to mitigate the risk of cascading RoLR failures. The AER will attempt to split customers among remaining registered RoLRs.

However, the AER notes that South Australia has only one local retailer with almost all connection points grouped to one TNI. In this instance, the AER could appoint one retailer to be the designated RoLR. However, depending on the volatility of the market, the appointment of one retailer may give rise to cascading failures. Therefore, if a TNI or distribution system approach is deemed not appropriate by the AER, AEMO and the state or territory; an alternative appointment approach will need to be determined between the AER, AEMO and the jurisdiction.

#### *Review of backup RoLR arrangements*

The AER proposes to review standing instructions to AEMO for backup RoLR arrangements every three years at the same time it reviews default RoLR arrangements. This process will take account of new additional RoLR offers but also changes in default RoLR customer bases over time.

Ad hoc reviews of backup RoLR arrangements will be triggered by events which also trigger default RoLR reviews.

#### *Broader policy issues*

It is likely that the provisions in the Retail Law may be insufficient to prevent cascading failures should a default RoLR fail in the absence of other market intervention. Under the Retail Law, all affected customers are required to be transferred to another retailer once a RoLR event occurs regardless of prices in the market. The AER encourages policy makers to further consider other emergency measures which may be used at the time of a RoLR event to prevent cascading failures.

#### **Draft RoLR statement of approach**

As proposed at section 3.7 of the AER's draft RoLR statement of approach, the AER sets out the following:

- Periodic review and ad-hoc review of backup RoLR arrangements—The AER proposes to review standing instructions to AEMO for backup RoLR arrangements every three years at the same time it reviews default RoLR arrangements. The AER proposes to conduct ad hoc reviews of backup RoLR arrangements when triggered by events which also trigger default RoLR reviews (or if an event affects a backup RoLR e.g. it fails).
- Preferred grouping of connection points—The AER proposes that standing instructions provide for the AER to designate customers to backup RoLRs on the basis of:
  - TNI (for electricity)
  - distribution systems (for gas)
  - if a TNI or distribution system approach is considered inappropriate by the AER, AEMO and jurisdiction, an approach determined between the AER, AEMO and jurisdiction.

## 2.2.6 General approach to the designation framework

If a registered RoLR goes on to be appointed as an actual RoLR for an event, the retailer is called a designated RoLR. The AER considers it important to define its general approach to the appointment of designated RoLRs and the application of the designation criteria under Part 6, Division 4 of the Retail Law.

The issues paper proposed an approach to appointment of designated RoLRs by reference to whether the AER had little notice (less than a few hours notice), short notice (up to 48 hours notice) or longer notice, in which to be able to advise AEMO of designated RoLRs under s. 132 of the Retail Law. The AER asked stakeholders what weight it should put on the prescribed designation criteria and what other criteria the AER should have regard to (if any). The AER enquired as to what information registered RoLRs could provide to confirm their ability to meet prudential requirements following the acquisition of customers at the time of a RoLR event. It also sought views on the information AEMO could provide at the time of a RoLR event and what other information could be sought from the failing retailer and potential RoLRs (and in what time frames) if there was longer notice of a RoLR event.

### *Effect of length of notice on designation decision*

AEMO welcomed the AER’s approach that if there is little notice of a RoLR event default RoLRs would be appointed as the designated RoLRs,<sup>10</sup> noting that this addresses the requirement for immediate RoLR implementation. The AER agrees it is important to have “ready to go” default RoLR arrangements. Therefore, the AER will provide standing instructions to AEMO as to who to transfer customers to should the AER have little time to consider other RoLR arrangements before a RoLR event. For situations where an AEMO suspension is the trigger for a RoLR event, AEMO

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<sup>10</sup> s.132 National Energy Retail Law

considered the AER would need to provide any instructions (different to standing instructions) by the time the retailer is required to respond to the call notice in electricity or the margin call in gas.

While the AER is able to notify AEMO of the designated RoLR anytime up until the occurrence of the RoLR event, the AER recognises this timeframe may not give AEMO adequate time to prepare its systems. Therefore, the AER considers a balance needs to be achieved between allowing AEMO to prepare adequately for a RoLR event and enabling the AER to make an informed decision regarding which retailer(s) should be the designated RoLR(s). To achieve this, the AER is proposing to use its best endeavours to notify AEMO who the designated RoLRs are by the time the retailers are due to respond to the call notice or margin call (or default notice in the event a call notice or margin was not issued). This decision has been reflected in the draft RoLR plan. However, the AER will maintain dialogue with AEMO regarding these timing arrangements to ensure the optimal outcome is achieved.

AGL queried whether the AER would ever have time to make a RoLR designation decision and therefore whether there was much to be gained from the complexity introduced by the registration of additional RoLRs. The AER considers that even where there is short notice e.g. 24 hours, if there are a number of firm offers to be an additional RoLR which are relevant to the RoLR event, the AER could provide notice on how to designate customers to AEMO shortly before the RoLR event.

Origin Energy considered that 24 hours notice may not be enough time for a RoLR to express interest in taking on customers at the time of a RoLR event and that 48 hours to 72 hours would be preferable if there were longer lead in times. The AER considers that there may be circumstances where more time could be provided to potential RoLRs, for example where market prices are stable and the business has sufficient guarantees to meet wholesale settlement requirements. In these circumstances, the AER will endeavour to provide additional notice.

The AER considers that if it has less than a few hours notice of a RoLR event it will rely on default RoLR arrangements advised to AEMO through standing instructions. With more than a few hours notice of an event, the AER will consider replacing standing instructions with a written notice, after taking account of AEMO information as to the affected customers and any additional RoLRs with firm offers who have agreed to take on customers without further consultation. If the AER has time, such as more than 48 hours notice of a RoLR event, the AER may call for expressions of interest as to terms and conditions on which registered RoLRs (all additional and default RoLRs) are willing to take on customers. The AER considers that if it does so, registered RoLRs should be given at least 48 hours to respond to a request for offers if time allows.

#### *Information sought based on contingency event powers*

The Retail Law provides for contingency event powers for the AER to seek more information from retailers where it thinks there are circumstances affecting that retailer which might lead to a RoLR event.<sup>11</sup> The purpose of these provisions is to

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<sup>11</sup> s. 130 National Energy Retail Law.

allow the AER and AEMO to potentially be informed before a RoLR event. The AER may also provide the information to registered RoLRs to assist them expressing interest as to terms of conditions on which they are willing to accept customers. The AER has significant discretion in exercising these powers, including which parties are informed about a potential RoLR event. A significant reason why the AER might not exercise these powers is if the AER has concerns that the exercise of these powers (particularly informing distributors or retailers) may bring forward a RoLR event by, for example, hampering a trade sale process (see discussion below).

The AER considers it important to provide guidance as to when it will exercise contingency event powers, and if it does so, what information will be sought under Division 3 of Part 6 of the Retail Law.

The AER expects that AEMO and retailers will, as required under s. 150 of the Retail Law, inform the AER whenever they have reason to believe there might be a RoLR event. This includes the reasonable belief of something which may give rise to some risk of a RoLR event. For example, the AER considers this requires AEMO to inform the AER anytime a margin call is issued in wholesale energy markets. Similarly, the AER expects that retailers would inform them immediately if they became aware of events, such as court proceedings or catastrophic system/plant failure, which may lead to a RoLR event.

When exercising contingency event powers, the AER will consider whether releasing information as to a likely RoLR event may preclude opportunities for a trade sale. Therefore before the AER releases any information of a RoLR event, acquired under Division 3 of the Retail Law or otherwise, it will consult with the retailer as to any relevant matters such as:

- whether the retailer is close to selling its customer base and
- whether there is a real likelihood of an injection of cash into the business.

The AER will generally attempt to provide the opportunity for a retailer to reach a commercial solution. However, where the AER considers that a RoLR event is likely and it can release information in a way which is unlikely to increase the risk of a RoLR event, it may release information for the purposes of RoLR event preparations. The AER will need to strike a balance between the risk of bringing a RoLR event forward and the benefits which could ensue from allowing more time for parties to prepare for a RoLR event. Some examples where releasing information may be unlikely to bring forward a RoLR event are if:

- a RoLR event is caused by an application to be wound up. In this case, for a listed company, a business may be required under the Corporations Act to declare the application such that the AER could make enquiries of registered RoLRs whether they would like to take on the failed retailer's customers
- a RoLR event involves a retailer effectively allowing itself to be suspended from an energy market, or
- the AER intends to revoke a retailer's authority.

Some of these examples reflect past RoLR events.<sup>12</sup>

### *Designation criteria*

In its issues paper, the AER sought views on which of the designation criteria the AER should give the most weight to. The designation criteria, listed in under s. 133(1) of the Retail Law, are:

- the RoLR criteria
- whether the registered RoLR has a cost recovery scheme and if so what costs are recoverable pursuant to that scheme and the amount or likely amount of those costs
- the imminence of the RoLR event, and
- any other matters the AER considers relevant in the circumstances.

Origin Energy considered that the RoLR criteria are likely to be the most important consideration. UED/Multinet also considered that where market prices are high the RoLR criteria should take precedence over other criteria such as RoLR event costs. Both noted that the first goal should be maintaining the integrity of the market by selecting a RoLR who would not itself fail. The AER agrees with these considerations.

In its issues paper, the AER listed event management, retail competition and the spreading of customers (to prevent cascading retailer failures) as other matters the AER may consider relevant in making its designation decision in accordance with s. 133(1)(d) of the Retail Law. UED/Multinet noted that the best solution might be one which leads to the selection of the fewest RoLRs, as this will make managing the RoLR event easier. However, a number of submissions, including UED/Multinet's, noted that for large retailer failures it may be important to spread a failed retailer's customers over a number of RoLRs to spread the risk and prevent cascading retailer failures. AGL's submission considered that the promotion of competition should not come at the expense of other overall RoLR scheme objectives, notably continuity of supply.

The AER agrees with submissions that the RoLR criteria will be the primary consideration at the time of a RoLR event, particularly determining whether a retailer has the financial resources to take on some or all of the affected customers.<sup>13</sup>

However, where the AER considers that two registered RoLRs equally satisfy the RoLR criteria it will be important to consider other designation criteria including whether one retailer has better RoLR cost recovery terms.<sup>14</sup>

For its designation decision, the AER considers that it will be important also to consider:<sup>15</sup>

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<sup>12</sup> Jackgreen RoLR event, Energy One RoLR event.

<sup>13</sup> s. 133(1)(a) National Energy Retail Law.

<sup>14</sup> s. 133(1)(b) National Energy Retail Law.

- any opportunities to simplify event management
- the need to spread customers over more retailers to prevent cascading failures and
- the effects on competition when choosing between registered RoLRs considered of similar merit against the designation criteria.

The AER notes that each of these further matters for consideration are directed at achieving the overall RoLR scheme objectives described at section 2.2.1. The degree to which these matters can be considered in addition to other designation criteria will depend on the imminence of the event.<sup>16</sup>

Simplification of event management may result in fewer delays or errors with customer information which is clearly in customers' interests. However, for larger retailer failures, the appointment of more designated RoLRs may reduce the risk that designated RoLRs themselves will in turn fail and better ensure the integrity of market arrangements. It follows that for large retailer failures, event management benefits from having one RoLR may be less important than the risk associated with cascading retailer failures if only one RoLR is designated.

Where registered RoLRs are willing to take on customers on equivalent terms under the designation criteria (eg. similar RoLR cost recovery terms), the AER may consider changes in market structure following the event. The AER may give preference to appointing the retailer with a smaller customer base provided it has the capacity to take on all the customers. In these circumstances, the AER considers that retail competition may be better promoted by the smaller retailer increasing its market share.

#### *Information about the failing retailer and information from potential RoLRs*

In its issues paper, the AER sought stakeholder feedback on the information AEMO could provide to support the AER's designation decision before a RoLR event.

AEMO noted that it could provide the following information about a failing retailer which could support an AER designation decision:

- TNI, local retailer area or NEM jurisdiction level customer number and load information for electricity
- jurisdictional and distribution system level gas customer number and load data and
- current and potential credit limits of potential designated RoLRs as well as existing guarantees.

AEMO further noted that the AER would need to assess the RoLR's ability to deliver additional guarantees if necessary. The AER and AEMO will progress the protocols required to receive this information to aid with designation decisions at the time of a

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<sup>15</sup> s. 133(1)(d) National Energy Retail Law.

<sup>16</sup> s. 133(1)(c) National Energy Retail Law.

RoLR event. If necessary, as AEMO suggests, the AER may seek information as to a RoLRs ability to deliver additional guarantees before a RoLR event.

### **Draft RoLR statement of approach**

As proposed at section 4.1 of the draft RoLR statement of approach the AER proposes the following approach as to which registered RoLRs will be considered for designation:

- With less than a few hours notice of a RoLR event—the AER proposes to rely on standing instructions to AEMO reflecting default/ backup RoLR arrangements.
- With more than a few hours notice of a RoLR event—the AER may provide written notice to AEMO to appoint additional RoLRs with firm offers who have agreed to be appointed without further consultation.
- With more than 48 hours notice of a RoLR event—the AER may consult with and seek expressions of interest from other registered RoLRs (including those with non firm offers) on terms and conditions on which they are willing to take on customers.

As proposed at section 4.3 of the draft statement of approach the AER will have regard to the following information to assist with its designation decision:

- With less than 48 hours notice—the AER will rely on information from AEMO before and at the time of a RoLR event, to be provided in accordance with an information protocol.
- With more than 48 hours notice—the AER may use contingency event powers to request information from retailers and registered RoLRs. The AER may exercise its discretion to inform registered RoLRs of a contingency event for the purposes of RoLR event preparations, where the AER considers that a RoLR event is likely and that it can release information in a way which is unlikely to increase the risk of a RoLR event.

As proposed at section 4.4 of the draft RoLR Statement of Approach the AER's approach to considering the designation will be:

- RoLR criteria—the AER will first have regard to whether a RoLR if designated is likely to satisfy the RoLR criteria. This will be the main consideration, along with any RoLR cost recovery scheme agreement, where standing instructions are relied on.
- Cost recovery schemes—the AER will give preference to appointing registered RoLRs whose offer can be identified as having lower costs recoverable under a RoLR cost recovery scheme.
- Other matters the AER considers relevant in the circumstances—where time permits the AER will also consider in making a designation decision:
  - opportunities to simplify event management
  - preventing cascading retailer failures, and

- changes to market share which support long term competition benefits.

## 2.2.7 Multiple RoLR appointments

Under s. 134 of the Retail Law the AER may appoint more than one designated RoLR for a RoLR event if the AER is of the opinion that it is appropriate to do so, having regard to the size of, or other circumstances surrounding, the event.<sup>17</sup> Under s. 135 of the Retail Law, the AER must specify in guidelines, the circumstances in which the appointment of more than one designated RoLR for a RoLR event may occur as well as the manner of determining the allocation of the designated RoLRs to customers.<sup>18</sup>

In the November 2010 RoLR appointments issues paper, the AER sought information on the matters it should consider in determining whether more than one designated RoLR should be appointed.

Concerning small or large retailer failures (not default RoLR failures), UED/Multinet recommended that there be one designated RoLR per electricity network area and per gas distribution system. It considered that it was important to keep the allocation of the RoLR simple and to maintain stability in the market. Other distribution businesses, SP Ausnet and Jemena, also considered that appointing an excessive number of additional RoLRs for a distribution system could lead to inefficiencies in the customer transfer process and confuse communications with customers.

The AER agrees that customer communication complications may increase as the number of RoLRs designated increases. Some potential exists for delays and errors in communications between distributors, RoLRs and customers. However, the AER notes that AEMO's electricity market systems support the grouping of customer data for RoLR designation by TNI, local retail area and jurisdiction and that AEMO has indicated it is able to group data in any of these three ways before sending it to distributors. The AER also considers that distributors should have systems which are capable of dealing with more than one retailer per local retailer area at the time of a RoLR event, consistent with their day to day operations in the electricity market. Further, before registering retailers as RoLRs, the AER will assess the organisational and technical capacity of a retailer to handle a RoLR event.

In appointing retailers as a designated RoLRs, the AER must consider the designation criteria under s. 133 of the Retail Law. These criteria provide the AER with discretion to take account of matters it considers relevant in the circumstances.<sup>19</sup> The AER set out a list of other matters it may consider at section 2.2.6 which are relevant to the appointment of multiple RoLRs. Accordingly, the circumstances where the AER might appoint more than one registered RoLR as the designated RoLR include:

- Where it appears the appointment of one RoLR may lead to cascading failure.
- Where the AER considers the appointment of a certain retailer as the designated RoLR for a certain area better satisfies the designation criteria. For example,

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<sup>17</sup> s.134(1) National Energy Retail Law.

<sup>18</sup> s. 135(2)(a),(b) National Energy Retail Law.

<sup>19</sup> s. 133 of the National Energy Retail Law



having regard to RoLR cost recovery terms, the AER may decide to appoint one designated RoLR for one area, and a different designated RoLR for a different area.

- Where the AER considers the appointment of multiple RoLRs will foster competition in the retail market and thus derive benefits for consumers.

In contrast, the AER is unlikely to appoint multiple designated RoLRs if one registered RoLR has terms and conditions superior to other registered RoLRs, e.g. no RoLR event cost recovery. Such an appointment would be conditional on the registered RoLR satisfying the designation criteria (encompassing financial resources).

#### **Draft decision on RoLR guidelines**

Section 2 of the draft RoLR guidelines sets out the AER's approach to when it may appoint multiple retailers as designated RoLRs in accordance with standing instructions to AEMO or in accordance with a written notice to AEMO at the time of a RoLR event.

#### **2.2.8 Grouping of customers for the purpose of designation**

Under s. 135(2)(b) of the Retail Law the AER must specify in RoLR guidelines the manner of determining the allocation of the designated RoLRs to particular customers or classes of customers.

The AER explored designation (and registration) possibilities against electricity connection points with AEMO through a series of meetings in 2010/2011 when market data system capabilities were discussed. Section 135(4) of the Retail Law requires that the AER consult with AEMO on the manner of determining the allocation of designated RoLRs. The grouping of electricity connection points by jurisdiction, local retail area or TNI were all identified as possible groupings. Using these groupings, AEMO would be able to provide wholesale market data and retail market data (i.e. information on the load profile and customer numbers) to RoLR participants with a high level of accuracy, and in reasonable time frames. Grouping by postcode was considered, but it was apparent that the data would be less accurate, with likely delays to customer transfer processes. For gas, AEMO informed that wholesale and retail market data could only be provided with a high level of accuracy and in reasonable time frames based at a gas distribution systems level.

In the issues paper, the AER sought comments on the grouping of electricity connection points for the purposes of registering and designating RoLRs. Origin Energy considered that the appointment of default RoLRs on a TNI basis may be more conducive to appointment of additional RoLRs and was not supportive of a single default RoLR per jurisdiction.

The AER considers that designation decisions may be made on a TNI basis depending on the circumstances of a RoLR event, for example if it is appropriate to split customers between a number of registered RoLRs to best guard against cascading retailer failures. However, the AER also considers in other circumstances that

designation in accordance with local retailer areas (e.g. under default RoLR arrangements) or by jurisdictions (e.g. one registered RoLR can take on all customers) may be appropriate. The AER's designation decisions will be made in consultation with AEMO.<sup>20</sup>

#### **Draft decision on RoLR guidelines**

As proposed at section 3 of the draft RoLR guidelines, the AER sets out its approach to the allocation of designated RoLRs to particular customers or classes of customers. This is based on TNI, Local Retailer Area and NEM Jurisdiction (in the case of electricity) and distribution system (in the case of gas).

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<sup>20</sup> s. 135(4) National Energy Retail Law.

## 3 RoLR cost recovery

### 3.1 Introduction

Under the Retail Law, a default or designated RoLR may seek to recover the costs it incurs in carrying out its obligations and functions under the RoLR scheme. The Retail Law provides that a default or designated RoLR may submit an application for a cost recovery scheme to the AER for determination. A cost recovery scheme allows a designated RoLR to recover its reasonable costs incurred following a RoLR event, and in the case of a default RoLR, in preparing for a RoLR event.

A cost recovery scheme also includes the mechanism, or combination of mechanisms, by which a RoLR will recover its reasonable costs. These could include upfront fees, retail variations or payments to the RoLR by distributors, who would then recover the costs of the payments from their customers.

The Retail Law provides that the AER may in the RoLR guidelines specify the form and information to be included in an application for a RoLR cost recovery scheme.

This chapter sets out the AER's draft decision on the cost recovery content of the draft RoLR guidelines in accordance with the requirements of Part 6 of the Retail Law.

This chapter also includes the AER's proposed approach on other issues important to the RoLR scheme cost recovery framework, including:

- the costs that are recoverable under a RoLR cost recovery scheme
- limitations on recoverable costs
- the assessment of RoLR benefits
- distributor recovery of the distributor payment determination and RoLR costs.

The AER's proposed approach on these issues is reflected in the draft RoLR statement of approach and will assist retailers understand the RoLR cost recovery framework.

### 3.2 Regulatory requirements

#### *Retail Law requirements*

Section 135 of the Retail Law sets out what the AER may include in the RoLR guidelines concerning cost recovery. The guidelines may (without limitation) specify the form of, and information to be included in, an application for a RoLR cost recovery scheme.

Part 6 Division 9 of the Retail Law sets out the framework for RoLRs to recover RoLR scheme costs incurred in preparation for and/or on and after a RoLR event. The

AER must, on application by a RoLR, make a cost recovery scheme determination and be guided by the following principles:<sup>21</sup>

- a) The registered RoLR should be provided with a reasonable opportunity to recover the reasonable costs it incurs with respect to the RoLR scheme
- b) The recovery of costs should allow for a return commensurate with the regulatory and commercial risks with respect to the RoLR scheme, and
- c) The registered RoLR will itself bear some of the costs, in proportion to its customer base.

The AER may in a RoLR cost recovery scheme determination, limit the costs that are recoverable.<sup>22</sup> The AER's determination may, so far as it relates to or affects tariffs, differ between customers and classes of customers.<sup>23</sup>

The AER must, as part of the RoLR cost recovery scheme determination, make a determination that one or more distributors are to make payments towards the costs of the scheme (distributor payment determination).<sup>24</sup> Distributors must make payments in accordance with their liability under the determination.<sup>25</sup> The Retail Law deems such payments to be approved positive pass through amounts under the National Electricity Rules (Electricity Rules) in the case of electricity, or approved cost pass throughs allowing variation of the distributor's tariffs (in the case of gas).<sup>26</sup>

### **3.3 Submissions received on the RoLR cost recovery issues paper**

In November 2010, the AER released an issues paper on its future responsibilities in administering the RoLR cost recovery framework.<sup>27</sup> In making the draft decision, the AER has considered the submissions received to the RoLR cost recovery issues paper, the cost recovery provisions in the Retail Law and the AER's decision-making framework under the Retail Law.

The AER received submissions from the following parties:

- ActewAGL
- AGL
- Citipower and Powercor (Citipower/Powercor)

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<sup>21</sup> s. 166(7) National Energy Retail Law.

<sup>22</sup> s. 166(8) National Energy Retail Law.

<sup>23</sup> s. 166(9) National Energy Retail Law.

<sup>24</sup> s. 167(1) National Energy Retail Law.

<sup>25</sup> s. 167(3) National Energy Retail Law.

<sup>26</sup> s. 167(4) National Energy Retail Law.

<sup>27</sup> AER, *RoLR Cost recovery scheme issues paper*, November 2010, <http://intranet.accc.gov.au/content/index.phtml/itemId/1234215>.

- Country Energy<sup>28</sup>
- Energex
- Energy and Water Ombudsman NSW
- Energy Networks Association (ENA)
- Envestra
- Ergon Energy
- ETSA Utilities (ETSA)
- Integral Energy<sup>29</sup>
- Jemena
- Origin Energy
- SP Ausnet
- United Energy Distribution and Multinet Gas (UED/Multinet)

The main issues raised were in relation to:

- the need for a cost recovery scheme to ensure the continuity and stability of the energy market
- the need for a cost recovery scheme to eliminate the costs of a RoLR event to a RoLR and any affected distributors
- the preferred cost recovery mechanism to recover RoLR costs
- how distributors would be able to recover their RoLR costs
- how the distributor payment determination should be apportioned between distributors and
- the types of costs incurred and benefits obtained by RoLRs and how the AER should assess such costs and benefits in determining the cost recovery scheme.

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<sup>28</sup> This submission was made by Country Energy prior to the NSW Government energy reform process in which Country Energy's retail business was sold to Origin Energy and Country Energy's electricity network business commenced operations under the name 'Essential Energy'. Thus, a reference to Country Energy in this notice of draft instruments refers to Country Energy prior to NSW Government energy reform process on 1 March 2011.

<sup>29</sup> This submission was made by Integral Energy prior to the NSW Government energy reform process in which Integral Energy's retail business was sold to Origin Energy and Integral Energy's electricity network business commenced operations under the name 'Endeavour Energy'. Thus, a reference to Integral Energy in this notice of draft instruments refers to Integral Energy prior to NSW Government energy reform process on 1 March 2011.

## 3.4 Draft RoLR guidelines: cost recovery issues

### 3.4.1 Form and information to be included in an RoLR cost recovery application

The AER may specify the form of, and information to be included in, an application for a RoLR cost recovery scheme. The AER proposes to exercise this discretion and has included in the draft RoLR guidelines a list of the information to be included in an application and a template outlining the form that information must be presented in.

#### *Information to be included in an application*

In the November 2010 RoLR cost recovery issues paper, the AER sought submissions on the type of information which should be included in an application for a cost recovery scheme.

Energex proposed the inclusion of a list of distributors which may be affected by the cost recovery scheme determination. The AER agrees and considers that if a RoLR applies to recover costs through the distributor payment determination, the application should propose the distributor or distributors from which it seeks to recover costs, the quantum or proportion of costs it seeks to recover from each distributor and the timing of payments made under the distributor payment determination.

Envestra considered the inclusion of historical unit-rate analysis<sup>30</sup> in cost recovery scheme applications inappropriate. The AER does not consider it necessary for historical unit-rate analysis to be included in a cost recovery scheme application. However, in making a cost recovery scheme determination, the AER must be guided by the principle that the RoLR be provided with a reasonable opportunity to recover the reasonable costs incurred with respect to the RoLR scheme. This requires the AER to assess the reasonableness of the costs sought to be recovered by the RoLR. Hence, for each category of cost sought to be recovered by the RoLR, information should be provided which verifies the cost and the reasonableness of the cost.

Origin Energy stated that information in a cost recovery application should include operating expenditure, energy purchase and risk management costs and IT expenditure.

Both Origin Energy and Envestra considered confidential information submitted as part of the cost recovery scheme application should be kept confidential. The AER notes that its treatment of information received in an application will be consistent with the *ACCC–AER Information policy: The collection, use and disclosure of information*.<sup>31</sup>

In determining the information to be provided in a cost recovery application, the AER considered responses outlining the type and nature of preparation costs, the RoLR event costs which would be incurred, the principles for separation of RoLR

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<sup>30</sup> Unit-rate analysis is a mechanism for comparing costs over time. By reducing costs to ‘costs per unit’ changes in costs can be compared from one period to another.

<sup>31</sup> A copy of this policy is available on the AER website at <http://www.aer.gov.au/content/index.phtml/tag/aerPublications/>.

preparation costs from business as usual costs, and the evaluation of customer benefits.

The AER notes the principles outlined by Energex and Origin Energy in assessing whether costs incurred by the default RoLR are RoLR preparation costs or alternatively business as usual costs. In the context of the cost recovery application, the AER considers an application for RoLR preparation costs should include supporting evidence showing the costs claimed by the RoLR would not have been incurred regardless of its responsibilities as a default RoLR.

The AER received submissions for and against evaluating RoLR benefits as part of the RoLR cost recovery scheme determination. The AER considers the assessment of RoLR benefits is consistent with the principles in s. 166(7) of the Retail Law (for reasons set out in section 3.5.1). Hence, RoLRs will be required to submit as part of an application, information which will assist the AER in determining RoLR benefits.

#### **Draft decision on RoLR guidelines**

As proposed in section 5.1 of the draft RoLR guidelines, a RoLR cost recovery application must contain the information set out in that section.

#### ***The form of the cost recovery application***

In the RoLR cost recovery issues paper, the AER sought submissions on the form in which information in a RoLR cost recovery application should be presented. Origin Energy considered the information requirements of the RoLR scheme should not be prescriptive and should not require benchmarking comparisons.

The AER considers the form requirements for cost recovery scheme applications should not be onerous. However, for the AER to make a cost recovery scheme determination consistent with the principles in s. 166(7) of the Retail Law, accurate, assessable cost information is required (see also section 3.4.2). Hence, the AER requires any cost information submitted by RoLRs in their cost recovery scheme application to conform to the cost information template attached to the draft RoLR guidelines.

#### **Draft decision on RoLR guidelines**

As proposed in section 5.2 of the draft RoLR guidelines, the cost information for a RoLR cost recovery scheme application must conform to pro-forma template in Appendix D.

### **3.4.2 Matters the AER considers necessary with respect to the RoLR scheme**

Section 135(5)(c) gives the AER the power to provide in the RoLR guidelines for any other matter the AER considers necessary with respect to the RoLR scheme. The AER considers the following matters necessary with respect to the RoLR scheme and has addressed them in the draft RoLR guidelines:

- time limits for cost recovery applications
- limiting the recovery of RoLR event costs to ex-post recovery
- the consequence of submitting a cost recovery application which does not conform to the content and form requirements outlined in the RoLR guidelines.

The reasons why the AER considers such matters are necessary with respect to the RoLR scheme are outlined below.

***Timing limits for cost recovery applications***

In the RoLR cost recovery issues paper, the AER queried whether the AER should place restrictions in the RoLR guidelines on the time within which a RoLR may apply for a cost recovery scheme. Views were also sought on the appropriate time limits for RoLR event costs applications and RoLR preparation costs applications.

Ergon Energy supported the AER including time limits for cost recovery applications for RoLR event costs and submitted that, as far as practicable, the time frame for applications be consistent with existing pass through provisions. The AER notes the alignment of time frames with existing pass through arrangements is difficult given a RoLR event may occur at any time. If the distributor payment determination is made, the AER will endeavour to make timelines for RoLR recovery of costs consistent with distribution recovery timelines to ensure a timely recovery of costs.

No submissions raised objections to imposing a time limit on applications for either RoLR preparation or RoLR event costs.

The AER has included in the draft RoLR guidelines time limits for RoLRs to submit cost recovery scheme applications to recover RoLR preparation and RoLR event costs.

The AER considers the imposition of a time limit to submit a RoLR cost recovery application necessary. Lengthy delays make the substantiation of costs more difficult, which hinders the AER’s assessment of a RoLR’s cost recovery scheme application consistent with the guiding principles in s. 166(7). Further, the time limit supports the national energy retail objective as a timely resolution of RoLR scheme costs will help stabilise a post-RoLR event energy market. This promotes the long term interests of customers of energy with respect to quality safety, reliability and security of supply of energy for consumers.<sup>32</sup>

In determining the appropriate timeframes for RoLRs to submit cost recovery applications, the AER considered the responses to the issues paper.

Origin Energy considered a 9 month limit to submit an application for RoLR scheme preparation costs would be reasonable. The AER considers this is appropriate and therefore proposes that applications to recover RoLR preparation costs by default RoLRs be made no later than 9 months after being appointed as a default RoLR under the Retail Law.

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<sup>32</sup> s. 13 National Energy Retail Law.



The AER received submissions from AGL and Origin Energy about the appropriate time limit for an application for RoLR scheme costs incurred on and after the RoLR event. AGL commented that reasonable RoLR costs would take on average two billing cycles to identify. Origin Energy noted that in practice an application for cost recovery would likely be made within two months of a RoLR event. Nevertheless, Origin Energy considered that a time limit of 12 months would be reasonable. Given AGL's comments that all reasonable costs are identified within two billing cycles, the AER proposes a time limit of 9 months from the date of the RoLR event to make a cost recovery application for RoLR event costs. This should give the designated RoLR enough time to identify its reasonable costs and would allow a scheme determination to be made in most cases in less than a year after the RoLR event. This provides RoLR scheme participants with certainty about their RoLR scheme obligations and liabilities.

Origin Energy also considered any time limit should be flexible enough to allow for the recovery of costs identified after the application has been made. The AER considers a RoLR may apply for an amendment to be made to a cost recovery scheme under s.168 of the Retail Law. Issues surrounding the recovery of costs are discussed further in the next sub-section.

#### **Draft decision on RoLR guidelines**

As proposed in section 6.1 of the draft RoLR guidelines, the AER requires a RoLR to submit an application for recovery of RoLR scheme preparation costs within 9 months of being appointed a default RoLR under the Retail Law.

As proposed in section 6.1 of the draft RoLR guidelines, the AER requires a RoLR to submit an application for recovery of RoLR scheme costs incurred on and after a RoLR event within 9 months of the RoLR event in which the RoLR is appointed as a designated RoLR.

#### ***Limiting the recovery of RoLR event costs to ex-post recovery***

The AER considers it necessary to limit recovery of RoLR scheme costs incurred on and after a RoLR event to ex-post recovery (rather than ex-ante recovery). Under an ex-post framework costs are recovered after they become known. Under an ex-ante framework costs are estimated in advance.

Section 166(7) of the Retail Law states the RoLR should be provided with a reasonable opportunity to recover its reasonable costs and be provided with a return which is commensurate to the regulatory and commercial risks of the RoLR scheme. The national energy retail objective requires the AER to consider the long term interests of consumers of energy.

The AER considers an ex-ante cost recovery scheme for RoLR event costs is inconsistent with section 166(7) and the national energy retail objective. This is because, as Origin Energy's submission noted, the prevailing circumstances of a RoLR event and the costs which the RoLR will incur are difficult to foresee. An ex-ante cost recovery scheme would require the AER to make a determination when the RoLR scheme costs related to the RoLR event cannot be quantified or reasonably

estimated. Hence, an ex-ante cost recovery scheme may not provide the RoLR with an opportunity to recover its reasonable costs or provide a rate of return consistent with its RoLR scheme obligations. This is also not consistent with the national energy retail objective, as an ex-ante cost recovery scheme may be unable to deal with the unique circumstances of a RoLR event and safeguard against cascading retailer failure, which would compromise the long term interests of consumers of energy by further de-stabilising the energy market.

#### **Draft decision on RoLR guidelines**

As proposed in section 6.2 of the draft RoLR guidelines, a cost recovery scheme for the recovery of RoLR scheme costs incurred on or after a RoLR event is limited to ex-post recovery.

#### ***Consequence of submitting a non-conforming application***

The AER considers it necessary to outline in the draft RoLR guidelines the treatment of cost recovery scheme applications which do not conform to the guidelines' requirements. Compliance with the RoLR guidelines ensures that the AER has sufficient information before it to make a cost recovery scheme determination consistent with the principles in s. 166(7) of the Retail Law and the national energy retail objective.<sup>33</sup>

Section 166(2) of the Retail Law provides cost recovery scheme applications must conform to the content and form requirements of the RoLR guidelines. The Retail Law is, however, silent as to the effect of applications which do not conform to s 166(2). Given the importance of the adequate information to ensuring the AER makes a decision consistent with the principles in s. 166(7) and the national energy retail objective, the AER may refuse to assess an application until it is submitted in the prescribed form.

#### **Draft decision on RoLR guidelines**

As proposed in section 6.3 of the draft RoLR guidelines, the AER may refuse to assess an application until it is submitted in the form prescribed in section 5 of the guidelines.

### **3.5 RoLR scheme cost recovery framework issues**

#### **3.5.1 What costs are recoverable under a RoLR cost recovery scheme**

##### *Sources of RoLR scheme costs*

The Retail Law allows for recovery of costs incurred by the RoLR in relation to the RoLR scheme.<sup>34</sup> In the November 2010 RoLR cost recovery issues paper, the AER

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<sup>33</sup> s. 13 National Energy Retail Law.

<sup>34</sup> s. 166(3) National Energy Retail Law.

sought submissions on the likely sources of preparation and incremental RoLR costs incurred on and after a RoLR event.

AGL listed the likely sources of preparation costs as the costs of:

- ensuring retailer systems have the capability and capacity to deal with a RoLR event
- putting financial resources in place to ensure the retailer has the ability to act as a default RoLR
- putting in place documentation and procedures for a RoLR event and
- testing of systems and procedures to manage a RoLR event (if significant).

AGL listed the likely sources of incremental RoLR scheme costs incurred on and following a RoLR event as:

- wholesale energy purchase costs greater than the costs covered by the standing offer tariff
- increased financing costs
- meter reading costs
- administrative costs of incorporating customers in the RoLR's billing system
- service order costs and
- costs for communicating information on the RoLR event to transferred customers.

The AER considers these are the type of costs which are recoverable under the RoLR cost recovery scheme.

#### *Recovery of reasonable costs*

Section 166(7)(a) of the Retail Law provides that the RoLR be given a reasonable opportunity to recover its reasonable costs. The AER received several submissions commenting on how the AER should assess the reasonableness of RoLR scheme costs.

Energex considered the AER should apply normal regulatory processes to determine the efficiency of costs. Origin Energy submitted, however, that given the circumstances surrounding a RoLR event, the AER should not apply an efficiency test when assessing costs. Origin Energy recognised while there was a need for oversight of costs, the assessment of costs should focus on the reasonableness of costs, under the specific circumstances. The AER agrees that given time constraints and inherent difficulties in predicting RoLR scheme costs, it is not reasonable to limit designated RoLRs to the recovery of efficient costs for RoLR scheme costs incurred on and after the RoLR event.

To assess whether the RoLR scheme costs incurred on and after a RoLR event are reasonable, the AER will assess whether the actions of the designated RoLR in performing its obligations have been prudent to minimise the costs incurred in the circumstances. For example, if the designated RoLR has responded in a timely manner to a RoLR event by seeking to enter into hedging arrangements then such costs will likely be considered reasonable. Practically this may require the RoLR to provide the AER with documents supporting its decision-making processes.

However, the AER does not consider this approach is appropriate for preparation costs. The default RoLR will have sufficient time to scope and plan the work it needs to undertake to prepare for a RoLR event. In this case the AER considers it reasonable that the recoverable preparation costs be limited to a default RoLR's efficient costs. Accordingly, the AER may scrutinise preparation costs more closely than costs incurred on or after a RoLR event.

Origin Energy further commented that the assessment of the reasonableness of costs should include consideration of the willingness of a retailer to volunteer as a RoLR, with a lack of interest indicating insufficient risk weighted return to the supply side of the market. The AER considers while this may be a valid consideration when determining the return to provide a RoLR under s. 166(7)(b), it is not appropriate to take into account when assessing whether the costs incurred are reasonable. The AER notes a lack of willingness to volunteer as a RoLR may be driven by factors other than a lack of commercial interest. For example, small-medium retailers interested in volunteering as a RoLR may be unable to do so as they cannot meet additional prudential requirements or do not have systems in place to accept bulk customer transfers.

Envestra considered the interpretation of reasonable costs to be subjective, varying on a case-by-case basis. Envestra called for the AER to set up a dispute resolution mechanism to settle disputes between a RoLR and the AER about what costs are reasonable. The AER agrees with Envestra that what constitutes reasonable costs may vary on a case-by-case basis. However, the AER notes that it does not have the ability under the Retail Law to set up a dispute resolution mechanism.

#### **Draft RoLR statement of approach**

The AER's draft decision on the assessment of RoLR scheme costs is incorporated into the general principles for cost recovery scheme determinations in section 5.1 of the draft RoLR statement of approach:

- The AER considers RoLR scheme costs incurred on and following a RoLR event are reasonable if in incurring those costs, the RoLR has acted prudently to minimise costs.
- The AER considers RoLR scheme costs incurred in preparation for a RoLR event are reasonable if they are efficient.

#### *Benefits*

The RoLR cost recovery issues paper sought submissions on whether the AER should consider benefits accruing to a designated RoLR following a RoLR event in making a

cost recovery scheme determination. The issues paper noted a designated RoLR may derive benefit from a RoLR event from increasing its customer base without incurring the usual marketing costs. It may also derive benefits from improved economies of scale.

In response to the issues paper both AGL and Origin Energy submitted the potential benefits accruing to the RoLR would be difficult to calculate. For example, churn rates are likely to be higher for transferred customers than for the RoLR's existing customers. Origin Energy also submitted the benefits are overstated. On the other hand, Energex and the Energy and Water Ombudsman of NSW submitted the AER should take benefits into account and place a value on those benefits.

The AER considers that the consideration of benefits when making a RoLR cost recovery scheme determination is consistent with the principle that the RoLR be provided with a reasonable opportunity to recover its reasonable costs.

The AER considers in most cases, it is the 'net costs' of the designated RoLR that are relevant. The revenue that the designated RoLR earns from its transferred customers during the same period in which the RoLR scheme costs are incurred should be offset against the RoLR scheme costs.

In some circumstances, the AER may also factor in longer-term revenue obtained from transferred customers by the designated RoLR. If a retailer has managed to retain valuable customers from a RoLR event the AER will consider off-setting the net present value of those customer contracts (if the net present value is significant enough, it may mean that the designated RoLR cannot recover any costs). This approach reflects that these customers may be valuable for the designated RoLR, in particular once the retailer has had time to adjust its hedging strategy to "cover" the additional customers. The AER accepts that it may be difficult to place a net present value on the customers gained through a RoLR event, in particular since there is some suggestion that customers gained through RoLR events are more likely to "churn" away from the designated RoLR. Therefore, if the number of transferred customers is low or it appears that the net present value of the transferred is unlikely to be significant, it is less likely the AER would consider these longer-term factors.

#### **Draft decision on RoLR guidelines**

The AER requires benefits be taken into account when determining the quantum of the costs which a designated RoLR can recover under a RoLR cost recovery scheme determination.

### **3.5.2 Limitations on recoverable costs**

Section 166(8) of the Retail Law allows the AER to limit the cases or classes of cases of RoLR costs which are recoverable. In the RoLR cost recovery issues paper, the AER sought submissions on the limits that may be imposed on recoverable costs.

ActewAGL, AGL and Origin Energy generally considered the AER should not place limits on the recovery of RoLR costs beyond the limitations existing in the Retail Law. Origin Energy's submission expressed a preference for a time limit of no less than six months instead of three for the recovery of incremental wholesale energy

purchase costs, given the impact of a RoLR event on the wholesale market, the availability of settlement data and other sources of uncertainty. If a limit of three months was imposed, Origin Energy considered that cost recovery should recognise the additional costs which are borne by the RoLR in entering into short term hedging arrangements.

The AER considers it will generally not impose limits on the magnitude or classes of costs which are recoverable under the RoLR scheme. The AER recognises the role of cost recovery in preventing cascading retailer failure. However, the AER notes the limitations on cost recovery outlined in the Retail Law, namely that the RoLR scheme costs that are recoverable are those which are reasonable<sup>35</sup> and that the RoLR itself bear some costs in proportion to its customer base.<sup>36</sup>

The AER does not agree with Origin Energy that a six month time limit for the recovery of incremental wholesale energy costs is appropriate. The time period over which incremental wholesale and energy costs are recoverable will depend on the circumstances following the RoLR event and the reasonableness of including such wholesale and energy costs. The AER generally considers that the further removed from a RoLR event, the less likely incremental wholesale energy and incremental costs will be considered a RoLR scheme cost.

In relation to Origin Energy's other concerns, the AER notes that previous RoLR events in Australia have not affected the availability of settlement data and it would generally be unnecessary for a RoLR to enter exclusively into short-term hedging arrangements to meet the additional energy requirements of transferred customers, particularly for small retailer failures. Submissions have noted the churn rate of transferred customers is higher than normal customer churn rates. However, unless the RoLR can show it was reasonable for it to assume a majority of the transferred customers will churn away from the RoLR in the months following the RoLR event such that long-term hedging is an unviable option, then the additional cost of short term hedging arrangements will not be fully recoverable.

#### **Draft RoLR statement of approach**

As proposed in section 5.1 of the draft RoLR statement of approach the AER will not generally impose limits on the magnitude of costs or classes of costs which are recoverable under a RoLR scheme.

### **3.5.3 Cost recovery mechanisms**

The RoLR cost recovery issues paper identified three possible cost recovery mechanisms—an upfront fee, a retail tariff variation and a distribution payment determination. The RoLR cost recovery issues paper sought submissions on the use of these mechanisms to recover costs and on other possible cost recovery mechanisms.

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<sup>35</sup> s. 166(7)(a) National Energy Retail Law.

<sup>36</sup> s. 166(7)(c) National Energy Retail Law.

### *Upfront fees*

UED/Multinet supported an upfront fee, but considered it may be problematic for the designated RoLR to recover its costs. Origin Energy stated upfront fees were inappropriate, as a failure to recover upfront fees is more likely following a RoLR event and the existence of the fee increased the likelihood of customers churning away before paying the up front fee. Origin Energy further noted in its experience, there was a material churn of transferred customers away from the designated RoLR. Jemena however considered an upfront fee was appropriate for small to medium retail failures, as the cost impact on customers would not be significant.

Generally, the AER does not consider that upfront fees are appropriate where it results in transferred small customers incurring significant upfront costs. It would be inconsistent with the AER's obligation to exercise its regulatory powers in accordance with the interests of the consumer protection of small customers<sup>37</sup> if the AER allowed such price shocks to occur. The price shock from an upfront fee may be particularly onerous for customers in financial hardship.

Moreover, if the upfront fee is onerous, it may, as Origin Energy suggests, increase the churn rates of transferred customers. In those circumstances, the use of an upfront fee may not provide the RoLR with a reasonable opportunity to recover its reasonable costs.<sup>38</sup>

### *Retail tariff variation*

AGL expressed concern that as retail regulation is still subject to jurisdictional control in most states, a complete pass through of costs by way of a variation to retail tariffs may be precluded. The AER notes it can only vary the retail tariffs of transferred small customers who are under RoLR deemed small customer retail arrangements.<sup>39</sup> Consequently, the use of the retail tariff variation cannot be used by default RoLRs to recover RoLR scheme preparation costs as the tariffs which the AER can vary only come into effect after a RoLR event.

Jemena supported the use of the retailer tariff variation to recover costs in small to medium retailer failures and considered it was unlikely to drive away customers as the retail tariff increases were unlikely to be significant. The AER considers in practice this may present some challenges. The RoLR deemed small customer retail arrangement noted above only lasts three months from the transfer date.<sup>40</sup> As cost recovery is limited to ex-post recovery (section 3.4.2) by the time the cost recovery determination is made following the RoLR event, the retailer may only have a limited window to recover costs through the retail tariff variation. This may result in significant price increases, increasing the likelihood of transferred customers churning away from the retailer.

Country Energy considered a retail tariff variation would be the most appropriate cost recovery mechanism as it allows for the quickest recovery of costs over a large

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<sup>37</sup> s. 205 National Energy Retail Law.

<sup>38</sup> s. 166(7)(a) National Energy Retail Law.

<sup>39</sup> s. 145(4) National Energy Retail Law.

<sup>40</sup> s. 145(4) National Energy Retail Law.

customer base. The AER notes a retail tariff variation does not guarantee a large customer base to recover costs. The tariff variation only applies to transferred customers under a RoLR deemed small customer retail arrangement and transferred small customers are not required to stay on the arrangements for any period of time. Therefore, the customer base from which the RoLR can recover its costs will be dependent on the number of transferred customers and the length of time before customers churn away from the RoLR following the event.

### *Distributor payment determination*

AGL and Origin Energy considered that distributor payments are the most appropriate cost recovery mechanism.

Envestra submitted that as distributor payments allow the costs of a RoLR event to be recovered from a much broader customer base, the burden of cost recovery experienced by individuals is much smaller. UED/Multinet made similar submissions. Envestra also argued that distributor payments may also provide the RoLR with an improved ability to recover all of its costs as it does not recover costs only from customers of the failed retailer.

ENA did not believe that distributor payments should be the sole cost recovery mechanism. It argued that the AER should take into account any lower tariff or other financial advantage customers received when they were customers of the failed retailer to ensure that those customers bear a reasonable amount of the RoLR costs. Jemena and SP Ausnet made similar submissions.

The AER considers there are times when the sole use of the distributor payment determination is appropriate. Where RoLR scheme costs are significant, the distribution determination allows costs to be spread over a broad customer base, minimising the financial impact on individual customers. The AER also considers the RoLR scheme in part provides for market integrity and security following a retailer failure. Given this function, it is appropriate that where significant RoLR scheme costs are incurred, a broader base of customers contribute to the recovery of these costs, particularly where a RoLR event may detrimentally affect the long term operation of the market.

Jemena submitted distributor payments should only be considered as an appropriate cost recovery mechanism in cases where the failed retailer is large. The AER considers the use of the distributor payment determination should not be limited to large retailer failures. In determining the appropriate cost recovery scheme, the AER will be driven by the need to ensure the cost recovery mechanism is consistent with the principles in s. 166(7) of the Retail Law, promotes the objectives of the National energy retail objective<sup>41</sup> and provides for the protection of small customers.<sup>42</sup>

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<sup>41</sup> s. 13 National Energy Retail Law.

<sup>42</sup> s. 205 National Energy Retail Law.



### *Other mechanisms*

ActewAGL considered it is preferable to develop a mechanism that spreads the cost of a RoLR event across the national market. To achieve this ActewAGL submitted the development of a national insurance scheme could be considered as an option. ETSA submitted a more equitable approach (to the ones raised in the issues paper) would be for the RoLR to recover its costs through increased fees payable to AEMO by all retailers. As an alternative, ETSA proposed the establishment of an insurance fund, which would be funded by a levy on all retailers, to meet the costs of RoLR events.<sup>43</sup> The AER considers, however, that development of either of these mechanisms is outside its functions and powers under the Retail Law.

#### **Draft RoLR statement of approach**

As proposed in section 5.1 of the draft RoLR statement of approach the AER proposes as general principles for cost recovery scheme determinations that:

- up front fees should not result in significant price shocks for customers
- the recovery of costs should not be limited to customers of the failed retailer
- cost recovery should occur over the largest customer base which is appropriate to the circumstances.

#### **3.5.4 Distributor liability for the distributor payment determination**

The RoLR cost recovery issues paper invited submissions on what considerations should be taken into account by the AER under section 167(3) of the Retail Law when determining distributor liability for the distributor payment determination.

Ergon Energy and AGL submitted that if a RoLR event occurs across multiple distribution areas, cost recovery could be based on the number of customers for each distribution network. AGL acknowledged while this is more administratively complicated than recovering all costs from just one distributor, it is a more equitable approach.

Jemena and UED/Multinet considered the AER should give consideration to minimising the cash flow impacts on distributors when making the distributor payment determination. Jemena added that where a large retailer failure occurs, use of the distributor payment determination may cause short term funding constraints. Envestra stated that if the failed retailer operated across different distribution networks and jurisdictions, then allocation of all costs to one distributor may present an unacceptable financial burden for that distributor. Envestra considered that flexibility was needed and that costs should be allocated to more than one distributor, depending on the circumstances.

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<sup>43</sup> Under ETSA's proposal, once the fund reached a pre-determined limit, the levy would cease and any earnings either re-invested in the fund or used to reduce the fees payable to AEMO.

SP Ausnet considered distributors should not pay for RoLR costs as it would require additional funding which is more expensive than the cost of capital for planned network expenditure. As a publicly listed company, SP Ausnet was further concerned about the business impact the RoLR scheme may have on it, as it may increase the risk profile of the distributor and could deter shareholder investment.

Energex submitted that costs should be apportioned to distributors on the basis of the number of the failed retailer's customers connected to each distribution network. Ergon Energy submitted that allocation of costs could be based on customer numbers, energy usage or a hybrid approach, depending on the nature of the costs. Ergon Energy further considered that, from a materiality perspective, a case could be made for all costs to be allocated to one distributor if that distributor's share, based on customer numbers, exceeds a certain percentage, for example 90 per cent. Jemena and Origin Energy made similar submissions, with Jemena proposing a threshold of 80 per cent.

The AER will take into account any potential financial impacts which the distributor payment determination may have on distributors and will consult with affected distributors prior to making a determination. If the distributor payment determination is likely to cause short term funding constraints on distributors, the AER will consider spreading the payment liability of the distributor payment determination among multiple distributors.

The AER generally considers where a retailer failure affects multiple jurisdictions, distributors will be appointed in each jurisdiction. This will minimise the short term financial impacts on distributors and allow for the recovery of costs over the largest customer base appropriate to the circumstances. The AER however notes the appointment of multiple distributors will be made on a case by case basis depending on the circumstances of the RoLR event. This would include the size of the failed retailer and whether it was active in more than one distribution area.

The AER will consider the allocation methodology used to apportion liability for the distributor payment determination on a case by case basis. Any allocation methodology will be fair and reasonable. The AER agrees with submissions that, if the cost allocation methodology results in one distributor being allocated the bulk of the RoLR costs, then that distributor should be allocated all the RoLR costs provided it does not impose an onerous financial burden on the distributor. The value of allocating small amounts of costs to other distributors would not justify the higher administrative costs involved in recovering those costs from the distributors' customers. The AER has not formed a view on a specific threshold, but will consider this matter on a case by case basis.

#### **Draft RoLR statement of approach**

As proposed at section 5.2 of the draft RoLR statement of approach, the AER considers:

- Apportionment of distributor payment determination between distributors will be decided on a case by case basis.

- Liability for the distributor payment determination should not result in onerous financial obligations on distributors.
- Generally if a retailer failure affects multiple jurisdictions, distributors will be appointed in each jurisdiction.

### **3.5.5 Distributor cost recovery**

#### *Distributor payment determination*

Section 167 of the Retail Law requires the AER to make a distributor payment determination as part of the cost recovery scheme determination. The AER received several submissions responding to the RoLR cost recovery issues paper seeking clarification on the interaction of distributor payment determination and the distribution framework.<sup>44</sup>

Ergon Energy submitted the AER should consider whether a positive pass through amount approved is the most effective and efficient cost recovery mechanism for a distributor to recover payments under a RoLR cost recovery scheme. The AER considers, however, that it does not have the power under the Retail Law to develop alternative mechanisms.

Country Energy and UED/Multinet sought clarification on how the distributor payment determination provisions would interact with the distribution framework. Ergon Energy further stated the AER should consider the appropriateness of distributors applying the pass through provisions to recover the distributor payment determination. Country Energy, Citipower/Powercor, Energex, Ergon Energy and Integral Energy also raised concerns about recovery of the distributor payment determination being prevented by the materiality threshold under the Electricity Rules or applicable gas access arrangements.

The AER notes the Retail Law automatically approves scheme payments as a cost pass through amount. Consequently, a distributor would not need to apply to recover the distributor payment determination or satisfy the materiality thresholds for cost pass throughs. For electricity, when a payment is made for RoLR cost recovery, s. 167(4)(a) of the Retail Law deems the equivalent of a determination under cl 6.6.1(d) of the Electricity Rules to be made. The electricity distributor would then factor the pass through into its next pricing proposal. Similarly for gas, once the payment is made to the RoLR it is deemed to be an approved cost pass through under the distributor's gas access arrangement. The gas distributor would then apply to have its tariffs adjusted to account for the distributor payment determination in accordance with the relevant provisions in their gas access arrangements. The AER considers that, when seeking to incorporate the payments made to the RoLR, the distributor should provide documentation to the AER confirming the amounts paid to the RoLR.

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<sup>44</sup> The distribution framework encompasses for electricity – The National Electricity Law, National Electricity Rules and distribution determinations made under the Electricity Law and Rules and for gas – The National Gas Law, National Gas Rules and gas access arrangements made under the Gas Law and Rules.

Jemena, SP Ausnet and UED/Multinet also sought clarification on whether the recovery of the distributor payment determination could include a time value of money component, given the lengthy delay in recovering the distributor payment determination. SP Ausnet further considered the cost of capital would be higher than the cost of capital for planned network expenditure. The AER considers the distribution framework allows for a time value of money component to be included in the recovery of the distributor payment determination by allowing a return at the approved weighted average cost of capital.<sup>45</sup> The AER considers this adjustment would be made and approved as part of the distributor's annual pricing proposal to the AER.

#### *Recovery of distributor RoLR costs*

The AER received several submissions from distributors enquiring as to how they would be able to recover their own costs incurred in preparing for, and during and following a RoLR event.

ActewAGL and Envestra submitted that the Retail Law did not allow pass through of the preparation costs which a distributor would incur in preparing for a RoLR event. Envestra considered it undesirable for the recovery of costs under proposed or existing cost pass through arrangements as it gives rise to regulatory uncertainty.

The AER agrees with ActewAGL and Envestra that the Retail Law contains no provisions for the recovery of a distributor's costs. The AER, however, considers it outside the scope of its functions and powers to develop a cost recovery mechanism for distributors. Distributors seeking to recover their own RoLR costs will have to rely on the existing distribution regulatory framework to recover costs.

The AER notes under the existing distribution regulatory framework, distributors can recover their RoLR costs through the following mechanisms:

- The National Gas (Retail Support) Amendment<sup>46</sup> and National Electricity (Retail Support) Amendment<sup>47</sup> introduced as part of the National Energy Customer Framework introduces a new pass through event for the recovery of unpaid distribution charges which a distributor may incur due to a retailer insolvency.
- RoLR event preparation costs which a distributor incurs can be recovered through its existing cost pass through arrangements. The distributor would need to comply with all relevant requirements under the applicable distribution regulatory framework, including meeting any definitional, timing or materiality thresholds. Alternatively, if preparation costs are expected to be incurred in the following regulatory period, distributors may apply for those costs to be included as part of its revenue allowance.
- Costs incurred in responding to a RoLR event may be recovered through existing cost pass through arrangements. The electricity and gas distributor would need to

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<sup>45</sup> Approved by the AER as part at the last review of the distributor's access arrangement (for gas) or revenue determination (for electricity).

comply with all relevant requirements under the applicable distribution regulatory framework, including meeting any definitional timing or materiality thresholds.

### **Draft decision on RoLR guidelines and Draft RoLR statement of approach**

The AER does not propose including any of the matters below in the draft RoLR statement of approach or draft RoLR guidelines, but notes for completeness its response to submissions.

- The AER considers s.167(4) of the Retail Law allows for the distributor to recover the distributor payment determination by deeming the payments, once made, to be a approved pass through. Once the distributor has verified making payment to the RoLR, it can incorporate the payment amounts into its tariffs for the next regulatory year. During this incorporation, the distributor may adjust the tariffs to account for the time value of money using the distributors approved regulatory WACC.
- The AER considers the National Gas (Retail Support) Amendment and National Electricity (Retail Support) Amendment introduce a new pass through event allowing for the recovery of unpaid distribution charges from a failed retailer following a retailer insolvency.
- The AER considers other RoLR costs may be recovered through existing pass through arrangements in the distributor's distribution determination (for electricity) or access arrangement (for gas).
- The AER considers RoLR preparation costs, in addition to being recovered under existing pass through arrangements, may also be included as capital and/or operating expenditure as part of the distributor's regulatory proposal (for electricity) or access arrangement proposal (for gas).

## 4 RoLR plan

This chapter sets out the AER's draft approach on the RoLR plan. It also responds to submissions received in response to the AER's RoLR plan issues paper, published in November 2010.<sup>48</sup>

### 4.1 Regulatory requirements

#### *Retail Law requirements*

The Retail Law requires the AER to develop, make and maintain RoLR plans. Section 162 (2) of the Retail Law states the RoLR plan is a plan for:

- the procedures to be followed by the participants in the event of a RoLR event, including direct communication with customers of a failed retailer
- regular exercises to be carried out by participants in the plan.

The AER is required to develop and maintain RoLR plans in consultation with AEMO and Ministers of participating jurisdictions. The AER must also ensure that RoLR plan participants are consulted in the development and maintenance of the plan. The RoLR plan is not subject to the retail consultation procedure.

Section 162(4) of the Retail Law defines the RoLR plan participants to be:

- AER
- AEMO
- registered RoLRs or registered RoLRs nominated by the AER
- the distributor or distributors nominated by the AER
- other parties nominated by the AER.

The Retail Law requires RoLR plan participants to use their best endeavours to:

- comply with the plan
- assist in the development and maintenance of the plan
- participate in regular exercises as provided in the plan.

Section 162(3) of the Retail Law also requires the RoLR plan to be consistent with the RoLR procedures. The RoLR procedures may be made by AEMO and can include (but are not limited to) procedures to deal with matters relating to the operation or

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<sup>48</sup> AER, *RoLR Plan Issues Paper*, November 2010, <http://intranet.accc.gov.au/content/index.phtml/itemId/1234215>.

implementation of the RoLR scheme, such as the transfer of customers from failed retailers to designated RoLRs.<sup>49</sup>

## **4.2 Submissions received in response to the RoLR plan issues paper**

The AER received submissions on the November 2010 RoLR Plan Issues Paper from:

- AEMO
- Energex
- Energy and Water Ombudsman NSW (EWON)
- Energy and Water Ombudsman (Victoria) (EWOV)
- Envestra
- Ergon Energy
- ETSA Utilities (ETSA)
- Jemena
- Origin Energy
- SP Ausnet
- United Energy Distribution and Multinet Gas (UED/Multinet).

Submissions were generally supportive of the AER's proposed approach to the development of the RoLR plan. They agreed with the AER that the RoLR plan should draw on the previous work of businesses and government to develop the Victorian RoLR manual. However, submissions also emphasised that a national RoLR plan will need to take account of jurisdictional differences. This remainder of this chapter considers the key issues raised by submissions in response to the RoLR plan issues paper and sets out the AER's intended approach.

## **4.3 Issues**

### **4.3.1 RoLR plan participants**

In the RoLR plan issues paper, the AER proposed to include all retailers and state and territory energy ombudsman schemes as RoLR plan participants. The AER also sought advice on who else should be included as a RoLR plan participant.

#### *Retailers*

The AER considered that by requiring all retailers to participate in the development of the RoLR plan, they will become fully aware of their responsibilities in the event they

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<sup>49</sup> s. 144 National Energy Retail Law.

become a failed retailer or registered RoLR. This is important since the actions of a failing retailer or designated RoLR is crucial to operation of the RoLR scheme.

In response, most businesses supported the inclusion of all retailers as RoLR plan participants. However, Ergon Energy considered retailers should be RoLR plan participants on a rotational basis because of the ongoing costs to comply with the plan.

The AER continues to propose that all retailers will be RoLR plan participants. In response to Ergon Energy's concerns, compliance costs are not expected to exceed the current costs required to satisfy jurisdictional requirements. RoLR exercises, which are potentially the biggest cost associated with being a RoLR plan participant, will only occur on a periodic basis and if deemed required by the AER.

#### *State and territory energy ombudsman schemes*

The RoLR plan issues paper also proposed the inclusion of State and Territory energy ombudsman schemes as plan participants. This was based on the crucial role State and Territory ombudsman schemes have in assisting customers of the failed retailer to resolve complaints.

In response, EWON and EWOV supported their inclusion as a RoLR plan participant. Origin Energy encouraged the participation of the energy ombudsman schemes, but suggested consideration needs to be given to how they will recover their costs. UED / Multinet disagreed with the inclusion of the ombudsman schemes. They suggested this on the basis that ombudsman schemes do not give effect to or facilitate the transfer of initial communication to the customer.

The AER will include energy ombudsman schemes as RoLR plan participants. RoLR event customer dispute resolution interlinks with the RoLR plan, because the plan includes strategies on how to communicate with customers on their rights and responsibilities under the RoLR scheme. Therefore, the AER considers the contribution of State and Territory ombudsman schemes in developing customer communication strategies is essential. In response to Origin Energy's concerns regarding the ombudsman's cost recovery, the AER considers this a matter for the energy ombudsman to consider. However, it is expected that the costs attributed to the participation as a RoLR plan, would not exceed those generally incurred by an ombudsman when it engages in a regulatory consultation process.

#### *Metering Data Providers*

AEMO proposed in their submission to include metering data providers (MDPs) as RoLR plan participants. AEMO considers MDPs should be included since they provide high volumes of data during a RoLR event.

The AER acknowledges the important role MDPs play during a RoLR event. However, regulators generally do not communicate directly with MDPs during a RoLR event and MDPs rarely engage with the customers of a failed retailer. Further, since many distributors have MDPs operating within their businesses, distributors should be able to sufficiently represent their views during RoLR exercises. Therefore the AER does not propose including MDPs as RoLR plan participants.



### *Energy departments*

In the issues paper, the AER did not propose the inclusion of energy departments from participating jurisdictions as a RoLR plan participant. The AER considered that energy departments may have participated in the development of the RoLR plan as representatives of the Ministers for the participating jurisdictions, negating the need for them to be a RoLR plan participant. However, the AER considers there is merit to considering energy departments and ministers as two separate parties for the purposes of the RoLR plan. Primarily, this is in recognition of the AER's need to communicate with both parties separately in the lead-up to and following a RoLR event. Further it will also facilitate the participation of energy departments in the AER's RoLR exercises. Based on these two reasons, the AER is proposing to include energy departments as a RoLR plan participant.

#### **Draft approach on RoLR plan**

The AER proposes to include all retailers, state and territory energy ombudsman schemes and energy departments of participating jurisdictions as RoLR plan participants.

#### **4.3.2 Data Custodians**

Data custodians (either distributors or AEMO) act as a depository for customer details, usually from second tier retailers. They have been established in some jurisdictions in recognition that the RoLR may not always be able to access customer data from the failed retailer.

In the RoLR plan issues paper, the AER sought views on whether current data custodian arrangements were working and whether data custodian arrangements should be introduced into other jurisdictions. The AER noted in the issues paper that during the 2009 Jackgreen RoLR event, the quality of data provided from these arrangements was considered poor.

In response, industry generally supported the continuation of current arrangements—whereby distributors act as the data custodian for electricity and AEMO acts as the data custodian for gas. However, Energex considered data capture and storage by distributors is not appropriate given the information requirements of retailers compared with distributors (i.e. payment and credit arrangements).

The AER has discussed data custodian arrangements with AEMO. Both parties agree that the further development or adjustment of data custodian arrangements should be progressed by AEMO. However, the AER will monitor and provide input into the development of these procedures to ensure the objectives of the RoLR scheme are upheld.

#### **Draft approach on RoLR plan**

The AER proposes that the further development or adjustment of data custodian arrangements should be progressed by AEMO.

### 4.3.3 RoLR communication requirements

In the RoLR plan issues paper, the AER proposed communication requirements upon RoLR plan participants in the lead-up to and following a RoLR event. This included obligations upon the failed retailer and designated RoLR to provide certain information to the customers of the failed retailer.

In response, submissions raised consistency with other RoLR scheme obligations and pre-RoLR event notifications as key RoLR plan issues. Other issues raised concerned utilisation of industry contact lists, measures to quickly notify large customers and recognition of jurisdictional-specific requirements—such as the prudential obligations pertaining to participants in different gas markets. These arguments have been accepted by the AER and have been reflected in the RoLR plan.

Many distributor submissions advocated the need for timing requirements to be clear and reflective of the independencies that exist within the RoLR scheme. For example, it was identified that the ability of an electricity distributor to provide the designated RoLR with customer details will depend on when it gets the NMI list from AEMO.

The AER accepts these views and has sought to ensure key interdependencies within the RoLR scheme are recognised and timing requirements are clear. However, there are instances where terms such as ‘as soon as practicable’ are used. Where these terms have been used, it has been done to reflect a legislative requirement or to demonstrate that because a condition precedent exists, a timing requirement is difficult to impose.

Some submissions argued that certain parties should be informed of proposed RoLR events in the interests of RoLR scheme preparedness. EWOV stated in its submission that it wants to receive prior warning from the AER in the lead-up to a RoLR event. Energex considers the AER should email participants reminding them to review their roles and obligations in a RoLR event whenever it is anticipated.

In accordance with AER’s contingency event powers under s.130 of the Retail Law, the AER may communicate to certain parties in the lead-up to a potential RoLR event. For example, if the AER has reason to believe there is a risk of a RoLR event the AER may notify:

- distributors
- registered RoLRs of whom the inquiries are made
- relevant default RoLRs; and
- such other person as the AER considers relevant.

In any such case, the AER must give notice of that belief and of the grounds for the belief of a RoLR event to AEMO and Ministers of participating jurisdictions. Therefore, the AER could, for example, notify EWOV if a retailer failed to satisfy its default notice.

The AER recognises the sensitivity surrounding the provision of this information to parties outside of the government and AEMO. In particular, if the market becomes aware there is a failing retailer, the ability of the failing retailer to complete a trade

sale may be affected. Therefore, in instances where the AER is made aware by the failing retailer that it is seeking to conduct a trade sale, the AER is unlikely to notify parties outside of AEMO or the government.

In other circumstances, the AER may use its contingency event notification powers to notify RoLR plan participants in the interest of readiness or to seek interest from additional RoLRs to be the designated RoLR.

Therefore, the AER does not intend to definitively state in its RoLR plan whether or not it will notify parties, in addition to AEMO or Ministers of participating jurisdictions, regarding the likelihood of a RoLR event. The RoLR plan will simply reflect the contingency event notification powers of the Retail Law. The AER will make the decision on who to notify based on the circumstances of the event.

#### **Draft approach on RoLR plan**

The AER's proposes communication requirements as set out in the draft RoLR plan.

#### **4.3.4 RoLR exercises**

In the RoLR plan issues paper, the AER sought stakeholder views on the scope and frequency of RoLR exercises. This included whether RoLR exercises should be desk-top (paper based) or whether AEMO and business' systems should be used to conduct a trial RoLR event.

UED/Multinet and SP Ausnet suggested RoLR exercises with system run-throughs will require cost recovery. Energex argued that RoLR exercises should be conducted in periods that are traditionally not busy. Envestra considered RoLR exercises needed to be planned with sufficient lead time and potentially run on jurisdictional basis.

The AER considers that RoLR exercises should test communications between RoLR plan participants leading up to and following the failure of a retailer. The AER considers a desk-top exercise should sufficiently test this capability. However if the AER identifies a need for a system run-through, RoLR plan participants will be consulted on the organisation and scope of such an exercise.

The AER proposes to conduct RoLR exercises periodically, with the first RoLR exercise to be undertaken in March 2012 after the AER's and AEMO's RoLR regulatory arrangements are finalised. The AER is not defining specific intervals for RoLR exercises to be conducted, since the AER believes exercises should be conducted on a needs basis only. However, the AER will seek to give RoLR plan participant six months notice before any future RoLR exercise is conducted.

#### **Draft approach on RoLR plan**

The AER's proposes the RoLR exercise to be a desk-top exercise and conducted on a periodic basis. The first RoLR exercise is scheduled to be undertaken in March 2012. The AER will seek to give RoLR plan participant six months notice before any future RoLR exercise is conducted.

# Glossary

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ACCC/AER Information Policy	ACCC–AER Information policy: The collection, use and disclosure of information, available from the AER’s website
RoLR appointments issues paper	Issues paper released by the AER in November 2010 on registration and appointment aspects of the RoLR scheme available from the AER’s website
call notice	Has the meaning given by s.10 of the National Electricity Rules.
RoLR cost recovery issues paper	Issues paper released by the AER in November 2010 on cost recovery aspects of the RoLR scheme available from the AER’s website
default RoLR	Has the meaning given in s. 122 of the National Energy Retail Law
designated RoLR	Has the meaning given in s. 122 of the National Energy Retail Law
margin call	With respect to the Declared Wholesale Gas Market, has the meaning given by s.200 of the Gas Rules. With respect to the Short Term Trading Market, has the meaning given by s.364 of the Gas Rules.
regulated entity	Has the meaning given in s. 3 of the National Energy Retail Law
RoLR guidelines	The RoLR guidelines developed by the AER under s. 135 of the National Energy Retail Law
RoLR plan issues paper	Issues paper released by the AER in November 2010 on RoLR plan aspects of the RoLR scheme available from the AER’s website
RoLR statement of approach	The RoLR statement of approach the AER is developing to assist industry under the AER’s approach to the RoLR scheme
small customers	Has the meaning given by s.5 of the Retail Law.
standing instruction	Is a notice from the AER to AEMO setting out the electricity and gas default RoLRs and the RoLRs in the event of first tier retailer failure.  Has the meaning given by s.10 of the Electricity Rules.
suspension notice	With respect to the Declared Wholesale Gas Market, has the meaning given by s.200 of the Gas Rules. With respect to the Short Term Trading Market, has the meaning given by s.364 of the Gas Rules.

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