



Final

Retailer of Last Resort statement of approach

November 2011

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Shortened forms

ACCC/AER Information Policy	<i>ACCC–AER Information policy: The collection, use and disclosure of information, available from the AER’s web site</i>
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
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
MCE	Ministerial Council on Energy
MSATS	Market Settlement and Transfer Solution
NEM	National Electricity Market
NMI	National Metering Identifier
Retail Law	National Energy Retail Law
Retail Regulations	National Energy Retail Regulations
Retail Rules	National Energy Retail Rules
RoLR	Retailer of Last Resort
TNI	Transmission node identifier

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 National Energy Retail Law (Retail Law),¹ National Energy Retail Rules (Retail Rules) and National Energy Retail Regulations (Retail Regulations), has been developed through extensive consultation by the Ministerial Council on Energy (MCE). The MCE has agreed that jurisdictions will work towards a common target commencement date of 1 July 2012.

The Retail Law makes provision for a national Retailer of Last Resort (RoLR) scheme to provide common arrangements across participating jurisdictions in case of retailer failure. Under this scheme, the AER is responsible for the registration and appointment of RoLRs and the determination of RoLR cost recovery schemes to allow for the recovery of RoLR scheme costs.

1.2 Purpose of RoLR statement of approach

Under the Retail Law, the AER is required to make RoLR guidelines. These guidelines may specify aspects of the registration and appointment framework (such as multiple RoLR appointment) and RoLR cost recovery (such as the information to be included in an application for a RoLR cost recovery scheme).

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

In particular, the draft RoLR statement of approach sets out:

- when the AER will call for expressions of interest to register as a RoLR
- 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
- how the AER may assess whether the RoLR scheme costs incurred by a default or additional RoLR are recoverable, and
- what the AER will consider when making a RoLR cost recovery scheme determination and distributor payment determination.

1.3 Structure of RoLR statement of approach

The RoLR statement of approach is structured as follows:

¹ Set out in the Schedule to the National Energy Retail Law (South Australia) Act 2011

- chapter 2 explains the objectives the AER has considered in developing the RoLR scheme;
- chapter 3 sets out the registration framework (registration occurs before a RoLR event);
- chapter 4 sets out the designation framework (appointment of designated RoLRs occurs at the time of a RoLR event) including the criteria the AER will apply; and
- chapter 5 gives details of cost recovery schemes and the process for RoLRs to apply for costs after a RoLR event.

2 Objectives of a RoLR scheme

The AER's development of the national RoLR scheme under Part 6 of the Retail Law must be done in a manner which will, or is likely to, contribute to the achievement of the National energy retail objective (retail objective).² The retail objective is:

to promote 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.³

The AER must also develop the RoLR scheme in a manner compatible with the development and application of consumer protection of small customers (including but not limited to hardship customers).⁴

The AER's RoLR scheme objectives are designed to promote the above objectives, and foster conditions where retailers, distributors and other energy industry participants are confident to participate in the RoLR scheme. These objectives are:

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

With these objectives in mind, the AER considers the RoLR scheme should:

1. result in the appointment of designated RoLRs with the financial and organisational capacity to carry out the role
2. minimise the risks of a designated RoLR itself failing shortly after being appointed as a designated RoLR
3. set out clearly how the appointment of designated RoLRs will be made
4. not discourage trade sale opportunities
5. not be unduly costly to administer
6. be able to be implemented quickly and simply.

² s. 205 National Energy Retail Law.

³ s. 13 National Energy Retail Law.

⁴ s. 205 National Energy Retail Law.

3 Registration Framework

3.1 General information

This chapter sets out the process the AER will use to register RoLRs and to ensure retailers are registered for all retailer failures including the failure of default RoLRs.

3.2 Expressions of Interest

The AER will call for expressions of interest (EoIs) from retailers to register as RoLRs (RoLR registration EoI) upon the commencement of the Retail Law.⁵ Following this initial call, the AER will seek EoIs for default RoLRs every three years or at such times it considers appropriate.⁶ For additional RoLRs, the AER will seek EoIs from retailers every year.

Retailers seeking registration as a default RoLR or additional RoLR will be required to complete a RoLR registration EoI form, set out in the RoLR guidelines and available on the AER's website at www.aer.gov.au. The RoLR registration EoI form seeks information from the retailers including whether they seek to attach terms or conditions to their registration (discussed in 4.4).

The RoLR registration EoI form sets out information that may be provided by a retailer to demonstrate it satisfies the RoLR criteria. The RoLR criteria require the retailer to demonstrate adequate financial resources, necessary organisational and technical capacity suitable to be the RoLR and any other matters the AER considers relevant.⁷ The AER must take the RoLR criteria into consideration when deciding whether to register RoLRs.⁸ However, the AER is not obliged to register retailers even though they satisfy or appear to satisfy the RoLR criteria.⁹

The AER may register a retailer as a default RoLR (as opposed to an additional RoLR) even if it has not submitted an EoI.¹⁰

The AER may register one or more retailers as additional RoLRs for each electricity connection point, and for each gas distribution system.¹¹ All authorised energy retailers from participating jurisdictions will be able to seek registration as an additional RoLR. However, a retailer can only be registered as an additional RoLR for connection points (electricity) or distribution systems (gas) for which it is not the default RoLR.¹²

⁵ This will be subject to any transitional arrangements applying to default RoLR arrangements.

⁶ s. 124(1) National Energy Retail Law.

⁷ s. 123 National Energy Retail Law.

⁸ ss. 125(6) 126(2) National Energy Retail Law.

⁹ s. 125(11) 126(9) National Energy Retail Law.

¹⁰ s. 125(5) National Energy Retail Law

¹¹ s. 126(1) National Energy Retail Law.

¹² ss. 126 (5) and (6) National Energy Retail Law.

The rest of this chapter considers specific registration requirements for default RoLRs or additional RoLRs, areas of registration and the publication of a RoLR register. Finally, the AER specifies its approach to designating RoLRs should a default RoLR itself fail (backup RoLRs).

3.3 Default RoLRs

The AER must ensure that a default RoLR is registered to each connection point in the case of electricity, and each distribution system in the case of gas. Default RoLRs are required to take on customers for electricity connection points and gas distribution systems they are registered against, in the absence of other instructions from the AER to AEMO before a RoLR event.¹³

Meeting RoLR criteria

Unlike additional RoLRs (see 3.4 below), the AER does not propose allowing default RoLRs to register conditionally to take on, for example, a certain number of customers. Instead, default RoLRs will need to be able to take all customers of the failed retailer in their registered area at the time of a RoLR event. Therefore, in appointing default RoLRs, the AER will need to consider a retailer's ability to access potentially large financial resources at short notice (such as to meet significantly increased prudential requirements) as well as business support and IT systems to accommodate the transfer of a large number of customers. This suggests that smaller retailers with smaller financial bases and business systems will not be suited to being default RoLRs.

Periodic reviews and ad hoc reviews of default RoLR arrangements

The AER will review default RoLR arrangements on a three yearly basis at the same time as it reviews backup RoLR arrangements (discussed at 3.7 below).

The AER notes there may be circumstances when default RoLR arrangements might need to be reviewed at other times, for example if the default RoLR itself fails or if there is merger activity in the market. In considering whether there is a need to review default RoLR arrangements outside the three-yearly reviews, the AER will consider whether there has been a material change in the market or a retailer(s) circumstances.

Calls for EoIs

The AER will generally call for EoIs at least six months before the three-yearly reviews are due. This is to provide time to consider who should be registered as default RoLRs based on EoIs, or who should be required to be the default RoLR, if necessary. However, in other circumstances such as the exit of a default RoLR from the market, the AER may need to call for EoIs in shorter timeframes.

Standing instructions to AEMO

¹³ s. 132(1) National Energy Retail Law.

The AER will provide details of the default RoLR arrangements to AEMO as part of its standing instruction. The standing instructions will inform AEMO which retailers are the default RoLRs and when they should be appointed as the designated RoLRs should a retailer fail. The standing instructions will also outline which default RoLRs will be transitioned from jurisdictional regimes to the national regime and which default RoLRs will be appointed and registered by the AER.

3.4 Additional RoLRs

A retailer may seek registration to be an additional RoLR for an electricity connection point or gas distribution system for which they are not the default RoLR.

In the event of retailer failure, the AER may appoint as the designated RoLR an additional RoLR instead of, or in addition to, the default RoLRs. However, the AER must consider whether the retailer continues to satisfy the RoLR criteria before it appoints the additional RoLR as a designated RoLR. Further, the AER must notify AEMO of the additional RoLR's appointment as a designated RoLR before the day on which customers are transferred. As a result, the scope of the AER to appoint an additional RoLR as a designated RoLR may be limited where the AER is given little notice of a RoLR event.

Therefore, the AER has developed measures that will assist the selection process for the designated RoLRs. This includes establishing two categories of additional RoLR registration—a firm offer category and a non-firm offer category. The firm offer registration category allows retailers to pre-commit to the terms and conditions under which they would be prepared to be appointed as a RoLR. This enables the AER to have the information it needs to quickly make appointment decisions and the prior agreement of retailers to make the appointments. The non-firm offer category enables retailers to register their interest to be a RoLR, but does not commit them to acting in that role. Retailers are able to register for either or both additional RoLR categories.

The remainder of this section considers the two categories of additional RoLR registration.

Additional RoLR with firm offer

An additional RoLR with firm offer commits to being a RoLR but with certain restrictions or conditions.

While any term or condition may be proposed by the AER or retailer, the AER has established standard terms and conditions which it considers reasonable for additional RoLR with firm offer registration. The standard terms and conditions are set out in RoLR registration EoI form. They include:

- 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 which distribution system/s 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. (The AER may limit the type of customer the RoLR acquires on the basis of National Metering Identifier (NMI) classification rather than the definition of small and large customers contained in s. 5 of the Retail Law.) 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.¹⁴
- 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 all or some of RoLR event costs.

The AER also requires retailers seeking to be registered as additional RoLRs with firm offers to agree to be appointed as designated RoLRs without first being consulted by the AER.

A retailer's offer will be valid for three months. At the end of this period, retailers will need to confirm their offer with the AER. This includes identifying whether any events or circumstances have materially affected the retailer's ability to satisfy the RoLR criteria.

Additional RoLR with non-firm offer

An additional RoLR with non-firm offer does not commit to accepting customers, but has indicated its interest in being a designated RoLR if an event occurs. It may also propose terms and conditions but, unlike an additional RoLR with firm offer, they are not binding. Any conditions of registration will inform, but not determine, the AER's appointment decision as the retailer will need to be notified prior to appointment. Although a registered RoLR's consent is not required for appointment,¹⁵ the AER considers that it is prudent to confirm that an additional RoLR with non-firm offer is still prepared and capable of being appointed on the terms and conditions it previously proposed.

Meeting RoLR criteria

Unlike default RoLRs (see 3.3 above), additional RoLRs may register on a conditional basis such as up to a maximum number of customers. Where such conditions exist, the AER will consider these in assessing the retailer's application to be registered (for example, whether the retailer's business systems support taking on the number of customers specified in a condition).

¹⁴ In accordance with current AEMO systems, customer class options for electricity are restricted to NMI (small/large) classifications within the MSATS system.

¹⁵ s. 132(4) National Energy Retail Law.

In the case of gas where there is no declared wholesale gas market or short term trading market, the AER will take into account the extent to which additional RoLRs have contractual arrangements in place to ship gas. The AER will consider the merits of each registration application before determining whether a retailer should be registered as an additional RoLR. In some cases, for example for small, isolated gas distribution networks, the AER may register additional RoLRs notwithstanding that the RoLRs do not have existing contracts in place. In those instances the AER will rely on its powers to direct distributors, transmission service providers, and gas producers to make available to the designated RoLR the failed retailer's contracted capacity and gas.¹⁶

Periodic review of additional RoLR registration

The AER will review the registration of additional RoLRs with firm offers every three months and additional RoLRs with non-firm offers every two years.

Ad hoc review of additional RoLR registration

The AER will undertake an ad hoc review of the registration of an additional RoLR if the AER becomes aware of events or circumstances that may or will affect the retailer's ability to satisfy the RoLR criteria.

Calls for EoIs

The AER will call for EoIs to be an additional RoLR in either the firm or non-firm category on a yearly basis.

3.5 Area of registration

The AER must register RoLRs on the basis of distribution system for gas and connection points for electricity. However, the AER may group electricity connection points including by transmission node identifier (TNI), local retailer area or jurisdiction. This section sets out the AER's approach to registering RoLRs in the NEM.

Default RoLRs—electricity

The AER will register electricity default RoLRs by grouping connection points to TNI, local retailer area or NEM jurisdiction. The AER's default RoLR registration approach will be guided by the AER's RoLR scheme aims and objectives, including maintaining the integrity of wholesale markets and the continuity of payments at the time of a RoLR event. This may mean that in many cases, the smallest of these grouping of connection points, TNI, is used in order to best ensure against cascading RoLR failures.

The AER will review the TNI arrangements for accuracy at least every three years in conjunction with the reviews of default and backup RoLR arrangements. If the AER

¹⁶ s. 137 National Energy Retail Law.

is advised of a change in TNI arrangements, such as the creation of a new TNI, the AER will update the arrangements immediately.

Additional RoLRs—electricity

For additional RoLR registrations, the AER considers it appropriate that additional RoLRs register by jurisdiction for electricity. This will not prevent additional RoLRs from proposing conditions on offers, such as the total customer numbers they are willing to take. The AER considers this will reduce complexity at the time of a RoLR event, whereby the amount of offer/registered area combinations are likely to be reduced enabling the AER to reach a designation decision sooner.

As noted earlier, a retailer can only be registered as an additional RoLR for connection points for which it is not the default RoLR.¹⁷ In situations where a retailer is the default RoLR for only some customers in a jurisdiction, it may also be registered to be an additional RoLR for the other customers in that jurisdiction.

3.6 RoLR register

Section 127 of the Retail Law requires the AER to maintain and publish on its website a register of RoLRs. 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.

The AER's RoLR register will set out the following information:

- retailer name
- registration classification
- jurisdiction
- registration area (for default RoLRs) and
- terms and conditions (summary only).

The RoLR register will be available at www.aer.gov.au. The RoLR register will be updated whenever there is a new registered RoLR or a change to a retailer's RoLR registration.

3.7 Backup RoLRs

Backup RoLR arrangements are not a category of registration under the Retail Law. These are practical arrangements the AER will determine based on registered default RoLRs and additional RoLRs. Backup RoLR arrangements are required in the event of the failure of a default RoLR(s).

Since only one default RoLR can be appointed to an electricity connection point or gas distribution system, it is necessary to provide an immediate instruction which

¹⁷ ss. 126 (5) and (6) National Energy Retail Law.

AEMO can implement should the default RoLR itself fail. Therefore, the AER will need to consider default RoLR failure scenarios in advance and advise AEMO which remaining default RoLRs/ additional RoLRs are to be appointed in these circumstances.

Periodic reviews and ad hoc reviews of backup RoLR arrangements

The AER will review backup RoLR arrangements on a three-yearly basis at the same time as it reviews default RoLR arrangements.

The AER notes that there may be circumstances when backup RoLR arrangements might need to be reviewed at other times, for example if a default RoLR or backup RoLR itself fails or if there is merger activity in the market.

Standing instructions to AEMO

The AER's standing instructions to AEMO will direct AEMO to transfer customers to one or more of the remaining default RoLR(s), or registered additional RoLRs, in the event of a default RoLR failure.

Grouping of customers

The AER will make backup RoLR arrangements by grouping default RoLR connection points by TNI (in the case of electricity) and by distribution system (in the case of gas). The AER's approach as to which TNIs or gas distribution systems to allocate to which registered RoLRs will be guided by the AER's RoLR scheme aims and objectives, including maintaining the integrity of wholesale markets and the continuity of payments at the time of a RoLR event.

4 Designation Framework

4.1 General information

The RoLR scheme specifies that default RoLRs are appointed as the designated RoLR at the time of a RoLR event unless the AER provides AEMO with written notice replacing those arrangements, before the event actually occurs.¹⁸ It follows that the appointment of any additional RoLR as a designated RoLR for a RoLR event will depend on the AER having sufficient notice to consider whether it is preferable to make an appointment decision which is different to default RoLR arrangements. To improve the ability of the AER to appoint additional RoLRs as designated RoLRs, the AER will have an information protocol with AEMO. The information protocol will cover the AER receiving information from AEMO, and also enable the AER to quickly notify AEMO of designation decisions.

The AER may also request information from retailers if a RoLR contingency event occurs, to assist with its appointment decision.¹⁹ A contingency event can include any material default by a retailer concerning its obligations under energy laws with respect to the payment of money, the provision of securities or otherwise of a financial nature.²⁰

When appointing the designated RoLRs, the AER must take account of the designation criteria.²¹ These aspects of the designation framework are discussed further below.

4.2 Which registered RoLR can be considered?

A major factor in the AER's selection of designated RoLRs for appointment will be the length of time the AER has to make the decision. Figure 4.1 below considers which registered RoLRs may be considered for appointment as designated RoLRs, according to the amount of notice the AER receives of an impending RoLR event. The example illustrates that the more warning the AER has, the more registered RoLRs it will be able to consider.

¹⁸ s.132 National Energy Retail Law.

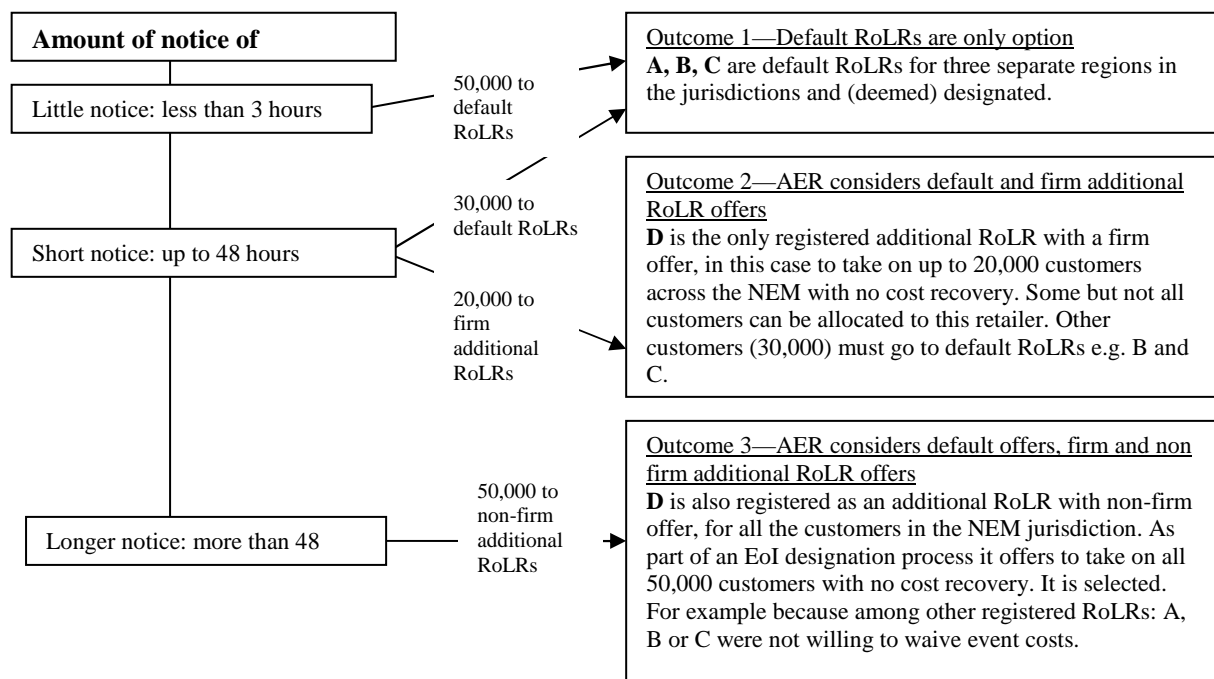
¹⁹ s.130 National Energy Retail Law.

²⁰ s.130(2) National Energy Retail Law.

²¹ s.133(1) National Energy Retail Law.

Figure 4.1 Which registered RoLRs may be considered?

Retailer X has 50,000 electricity customers across a NEM jurisdiction and there is a RoLR event.



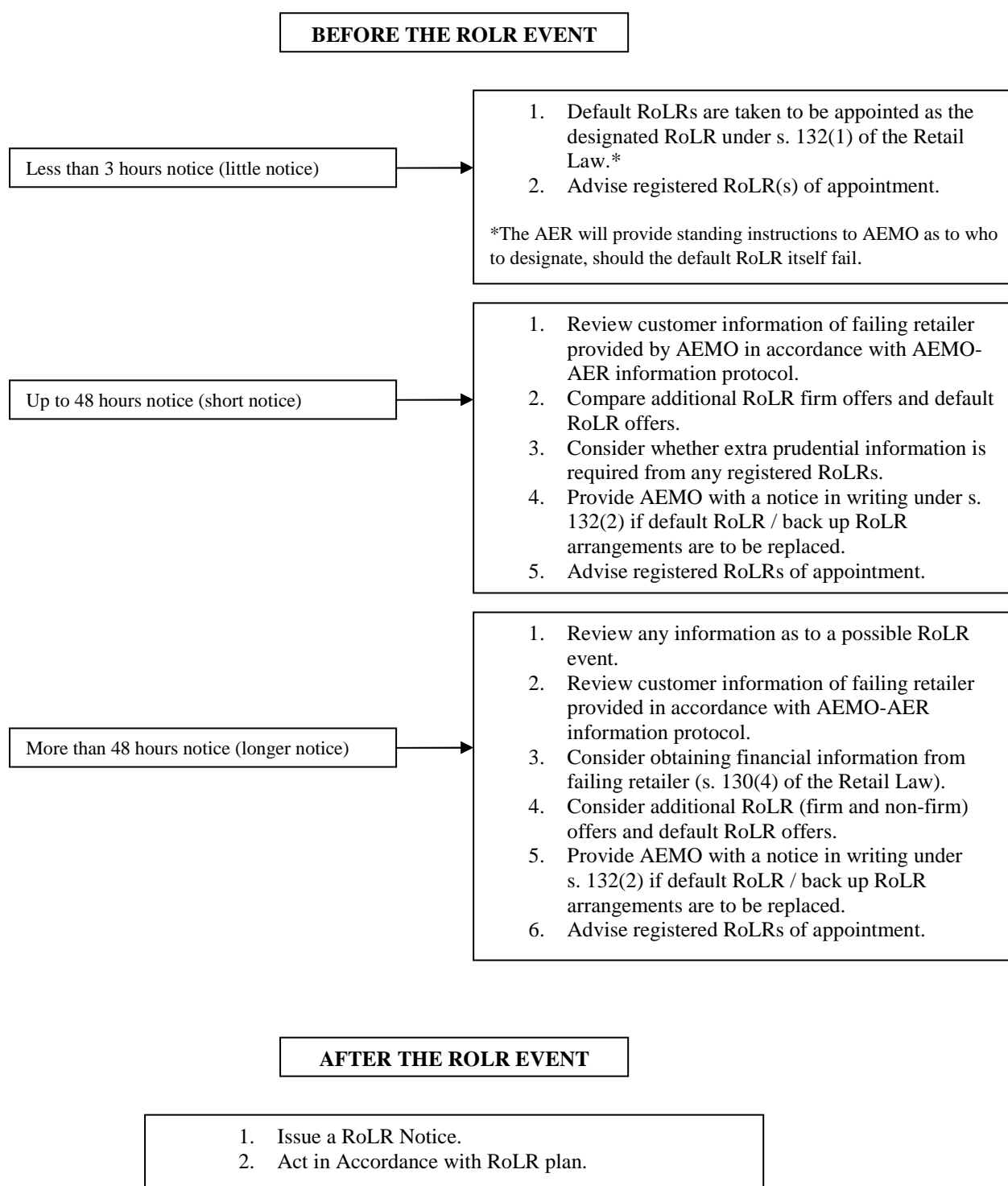
Outcome 1 shows that where there is less than a few hours notice of a RoLR event, the AER is most likely to appoint default RoLRs. Outcome 2 shows that with short notice (i.e. up to 48 hours) the AER may also be able to consider additional RoLRs with firm offers. Additional RoLRs with firm offers have agreed not to be consulted prior to being appointed as designated RoLRs (up to the maximum permitted by their terms and conditions).²² Outcome 3 reflects that where the AER has more than 48 hours notice of a RoLR event it may be able to consider (and consult with) other registered RoLRs. This would include non-firm additional RoLRs who have not agreed to be designated without further consultation at the time of an event.

4.3 Information flows

The information the AER will take account of, and the information it will provide before making a designation decision is highlighted in figure 4.2.

²² The AER notes that there would have been enough time with Australia’s two RoLR events for additional RoLRs with non-firm offers to have been considered. Energy One requested its suspension from the market and the Jackgreen suspension was triggered after a publicly announced creditors’ action to wind up.

Figure 4.2: RoLR information flows



Little notice

With little notice (less than 3 hours) of a RoLR event, the AER would not base its designation decision on any current information but would rely on default/backup RoLR arrangements.

Short notice

With short notice (up to 48 hours) the AER would have regard to the financial information provided by RoLRs during the registration process. The AER will also use information obtained from AEMO, in accordance with AEMO–AER information protocols, to consider at the time of an event:

- the number of customers affected and/or the load;
- the geographic location of the customers or load affected; and
- AEMO’s current prudential limits for registered RoLRs and their ability to absorb the new customer load.

The AER notes that a retailer’s current prudential limits may not accurately reflect its ability to take on extra customers following a RoLR event. Even if a retailer’s current prudentials (according to AEMO) are insufficient to absorb a certain number of customers or load, the retailer may be able to quickly increase its credit by obtaining further bank guarantees. If a RoLR appointment was likely to result in a retailer needing further credit (on the advice of AEMO), the AER would endeavour to satisfy itself that the retailer could secure the extra credit before appointing it as a RoLR.

Longer notice (use of contingency event powers)

In addition to considering information from AEMO, where there is longer notice (more than 48 hours) of a RoLR event, the AER may consider requesting information from the failed retailer and may explore the views of all registered RoLRs (including those in the non-firm offer category). The AER’s contingency event powers, under s. 130 of the Retail Law, enable the AER to seek more information from a retailer where it thinks there are circumstances affecting that retailer which might lead to a RoLR event.²³ These provisions potentially allow the AER, AEMO and other participants to be informed earlier of a RoLR event. These powers allow the AER to inquire with registered RoLRs about whether they want to be appointed as a designated RoLR in regards to a specific RoLR event.²⁴

The AER has discretion in exercising these powers, including which parties are given notice about a potential RoLR event.²⁵ However, the AER might not exercise these powers if it has concerns that the exercise of these powers (particularly informing distributors or retailers) may unintentionally provoke or bring forward a retailer failure. For example, 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

²³ s.130(4) National Energy Retail Law.

²⁴ s. 130(5)(a) National Energy Retail Law.

²⁵ s.130(5) National Energy Retail Law.

- there is a real likelihood of an injection of cash into the business.

The AER may request financial information from the retailer to ascertain its circumstances.²⁶ The kind of information the AER may request is set out at Appendix A.

The AER will generally endeavour to provide the opportunity for a retailer to reach a commercial solution which does not involve a RoLR event. However, where the AER considers that a RoLR event is likely, and it can release information in a way which is unlikely to worsen the situation for the retailer, it may release information for the purposes of RoLR event preparations. The AER will need to strike a balance between the risk of exacerbating the retailer's position, and the benefits which could ensue from allowing more time for parties to prepare for a RoLR event, including by making offers to take on customers. Giving notice of a potential RoLR event may be considered unlikely to bring forward a retail failure if:

- a RoLR event is caused by an application to be wound up, or
- a RoLR event involves a retailer effectively allowing itself to be suspended and deliberately exiting the market, or
- the AER intends to revoke a retailer's authorisation.

In these circumstances, the AER considers it could make enquiries of registered RoLRs as to whether they want to take on any of the failed retailer's customers. The AER would provide information to registered RoLRs as to the likelihood of a RoLR event and information about the likely customers involved.²⁷ The AER would then require the registered RoLRs it makes enquiries of, to submit EoIs within 48 hours through a tender process.

The form of enquiries that the AER would make of registered RoLRs as to whether they want to be appointed as a designated RoLR in the case of a RoLR event are set out in Appendix B.

The AER will exercise its discretion as to when to act under contingency event powers. However, 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. The AER notes 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 it issues a call notice in the NEM.

²⁶ The AER's powers to request information as to a retailer's financial circumstances, including by a regulatory information notice, are set out under Divisions 3 and 7 of Part 6 the National Energy Retail Law.

²⁷ The AER's power to pass on information to registered RoLRs is set out under subsection 130(5) of the National Energy Retail Law.

4.4 Application of the designation criteria

The AER will take into consideration the designation criteria before appointing a designated RoLR.²⁸ This section sets out how the AER may consider the designation criteria in accordance with how much notice of a RoLR event it receives.

Little notice

With little notice of less than 3 hours, the imminence of the RoLR event means that default/backup RoLR arrangements will be used. Default and backup RoLRs are likely to be larger retailers who were assessed against the RoLR criteria as able to take on a potentially large number of customers.

Short notice

With up to 48 hours notice of a RoLR event, the AER may be able to consider registered RoLR offers from additional RoLRs and default RoLRs. The AER might appoint registered RoLRs as designated RoLRs, rather than using the default / backup RoLR arrangements, if this resulted in some or all of the following:

- reduced likelihood of cascading retailer failures
- lower costs for customers, for example, if a retailer commits to take customers at a lower cost than a default RoLR
- the appointment of fewer designated RoLRs simplifying the event management process, and
- changes to market structure which support longer term competition benefits.

These are other relevant matters the AER would consider for the purposes of the criteria for RoLR designation. In particular, this would include the retailer's customer base and its financial capacity to purchase energy for the additional customers.

Longer notice

The more notice the AER has of an impending RoLR event, the more options it has to make RoLR appointments. The AER would seek offers from all registered RoLRs including default RoLRs and additional RoLRs.

Registered RoLRs would be encouraged to submit their best offers, having considered the information available at the time of the event. The AER notes that this extends to allowing additional RoLRs to vary their offers, for example in regards to how many customers they are willing to take, or in regards to RoLR cost recovery schemes.²⁹

When calling for EoIs, the AER suggests that retailers should be given at least 48

²⁸ As required under section 133 of the Retail Law.

²⁹ s. 133(2) Allows the registered RoLR and the AER by agreement to vary the RoLR's cost recovery scheme for the purpose of RoLR designation.

hours to respond to a request for offers, if time allows. The timeframe for the AER to appoint a RoLR will depend on the number of responses the AER receives. However, it anticipates that it would then make a decision within 48 hours. The criteria for RoLR designation that the AER would apply would be the same as for short notice considerations.

5 RoLR cost recovery schemes

This chapter sets out the general principles which the AER will consider when making a cost recovery scheme determination.³⁰ It discusses some hypothetical RoLR event scenarios, and proposes the RoLR cost recovery scheme and distributor payment determination the AER would consider consistent with the principles in s.166(7) of the Retail Law and the retail objective.

Under the Retail Law, a RoLR may apply to the AER seeking a RoLR cost recovery scheme determination to recover their RoLR scheme costs. Default RoLRs may apply to recover their RoLR scheme preparation costs³¹ and designated RoLRs may apply to recover their RoLR scheme event costs³². Default RoLRs must apply to recover their RoLR scheme preparation costs within nine months of being appointed as the default RoLR.³³ Designated RoLRs must apply to recover their RoLR scheme event costs within nine months of the relevant RoLR event.³⁴

The cost recovery schemes for the hypothetical RoLR event scenarios discussed below, are not binding on the AER's exercise of its powers. Rather, they serve as examples of considerations which the AER will take into account when exercising its powers under Part 6 Division 9 of the Retail Law. Under s. 166(1) of the Retail Law, the AER would need to make a cost recovery scheme determination for each designated RoLR that submits an application for a cost recovery scheme. This means, depending on the cost recovery application and the individual circumstances of each designated RoLR, different cost recovery schemes may apply for each RoLR for the same RoLR event.

5.1 General principles for cost recovery scheme determination

This section outlines the general principles which the AER will consider when determining a cost recovery scheme. The AER considers these principles are consistent with those outlined in s. 166(7) and s. 205 of the Retail Law. These general principles are not binding. However, if the AER does deviate from them in making a RoLR cost recovery scheme determination, it will provide reasons for its departure in the decision.

5.1.1 Assessment of reasonable costs

RoLR scheme costs incurred during and following a RoLR event

To assess whether the 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 and minimised the costs incurred in the circumstances.

³⁰ Under Division 9 of Part 6 of the Retail Law.

³¹ s. 166(3)(a) National Energy Retail Law.

³² s. 166(3)(b) National Energy Retail Law.

³³ cl. 6.1.1 RoLR guidelines.

³⁴ cl. 6.1.2 RoLR guidelines.

To assist the AER in its assessment, the designated RoLR should provide supporting documents of its decision-making processes.

RoLR scheme preparation costs

The AER considers it reasonable that the recovery of preparation costs be limited to a default RoLR's efficient costs.³⁵ The AER considers a default RoLR will have sufficient time to scope and plan the work it needs to undertake to prepare for a RoLR event. Accordingly, the AER will scrutinise preparation costs more closely than costs incurred on or after a RoLR event.

In assessing the efficiency of preparation costs, the AER may use a variety of approaches. Primarily, the AER will assess whether the default RoLR has sought to constrain their preparation costs. For example, when seeking to recover preparation costs associated with implementing IT system changes, the RoLR may produce documents of competitive tender processes from IT businesses or business cases as evidence the costs incurred were efficient.

5.1.2 Limits will not be imposed on the classes or magnitude of costs

As the RoLR should be provided with a reasonable opportunity to recover its reasonable costs incurred, and given the need to ensure the market integrity and security of the energy market following a RoLR event, limits on the classes or magnitude of costs will generally not be imposed.³⁶

5.1.3 Cost recovery mechanisms

Consideration of price shocks for small customers

The AER must perform its functions and exercise its powers in a manner compatible with the development and application of consumer protections for small customers, including protections relating to hardship customers.³⁷ Thus, cost recovery should not result in onerous price shocks for small customers, as this may present hardship issues for some customers. For this reason, the AER does not consider upfront fees are appropriate where the fee imposed is onerous for the transferred small customers of the failed retailer.

Extent of recovery of costs

The AER considers the RoLR scheme benefits all energy market participants, by providing market integrity and security following a RoLR event. Thus, the AER considers it appropriate that cost recovery extends beyond just the customers of the failed retailer.

³⁵ Section 166(3) of the Retail Law provides for default RoLRs only to recover costs incurred in preparing for RoLR events, and these should be reasonable costs under subsection 166(7). The Retail Law contains no provision for additional RoLRs, including backup RoLRs, to recover preparation costs.

³⁶ s. 166(7)(a) National Energy Retail Law.

³⁷ s. 205 National Energy Retail Law.

Consistent with the need to prevent significant price shocks for small customers, cost recovery should occur over the largest customer base which is appropriate to the RoLR event. The Retail Law provides for the spreading of the RoLR scheme costs of a RoLR event through the distributor payment determination.³⁸

5.2 General principles for the distributor payment determination

5.2.1 Consideration of the financial impacts of the distributor payment determination on distributors

Financial obligations imposed by the distributor payment determination on distributors

If a distributor is likely to have onerous financial obligations placed upon it by the distributor payment determination, the AER is likely to make a determination that more than one distributor is to make payments towards the costs of the RoLR scheme. The AER considers the short term financial impact of the distributor payment determination on any one distributor should be minimised, therefore any potential short term funding constraints as a result of making payments will be alleviated by spreading the payments over multiple distributors.

Appointment of distributors where retailer failure affects multiple jurisdictions

Where a retailer failure affects customers in multiple participating jurisdictions and the distributor payment determination is selected as a cost recovery mechanism, the AER will likely appoint distributors in each of the affected jurisdictions. This will minimise the short term financial impacts on distributors, and is consistent with the AER's cost recovery scheme general principle that costs should be recovered over the largest customer base appropriate to the circumstances.

5.2.2 Apportionment of the distributor payment determination between distributors

The AER will apportion the liability for distributor payment determinations on a case by case basis. Such an allocation must support the retail objective, support the AER's RoLR scheme objectives and take into account the financial impact on distributors.

5.3 Cost recovery examples for hypothetical RoLR event scenarios

5.3.1 Scenario one

Enduring Energy operates in NSW, supplying electricity to 10 000 small customers. Enduring Energy is unable to pay its debts. Due to failure to comply with a statutory demand, an order to wind up the company is made. This triggers a RoLR event and

³⁸ s. 167(1) National Energy Retail Law.

the default RoLR in each distribution area is taken to be the designated RoLR for the event.³⁹

Given the RoLR event is localised and the small size of the failed retailer makes it unlikely to threaten the security or integrity of the market, the AER considers customers of the failed retailer should pay a greater portion of the costs. This can be achieved through a cost recovery scheme comprising an upfront fee and the distributor payment determination.

The upfront fee would recover the administrative costs associated with the transfer of customers from the failed retailer to the default RoLR. The AER considers limiting the upfront fee to administrative costs prevents onerous financial obligations being placed on small customers.

The distributor payment determination would be used to recover other associated RoLR costs such as incremental energy costs not covered by the RoLR retail tariff, costs paid to the insolvency official and service order costs. Given the small size of the retailer failure, the distributor payment determination will be limited to distributors operating in NSW.

5.3.2 Scenario two

Optimal Power operates in Victoria, supplying gas to 8 000 small customers. Spitfire is a registered gas RoLR with a firm offer of up to 2 000 small customers and has agreed in advance to forego cost recovery. Optimal Power is unable to meet its prudential requirements and AEMO suspends its right to trade. This triggers a RoLR event. The AER appoints Spitfire as a designated RoLR for 1 850 small customers in one gas network,⁴⁰ with the default RoLRs in the other gas networks being the designated RoLR for the remaining 6 150 small customers.

A similar cost recovery arrangement for scenario one for the default RoLRs would be considered appropriate by the AER. As Spitfire has agreed in its expression of interest not to recover costs, it is prevented under s. 167(5) of the Retail Law from seeking to recover costs. However, the default RoLRs could recover their costs.

5.3.3 Scenario three

Equitable Energy operates in South Australia and Victoria supplying electricity to 40 000 customers and gas to 35 000 customers. Continuing systemic non-compliance with the Retail Law and Retail Rules by Equitable Energy, which the AER has been unable to resolve through administrative and court enforceable undertakings, leads to the AER revoking its retailer authorisation. This triggers a RoLR event. Prior to the revocation of its retailer authorisation, the AER has enquired with registered RoLRs about being appointed a designated RoLR. Ozzie Power, Dynamic Energy, Frontier Power, Magnificent Power, Focus Energy and People Power have agreed they will only recover the administrative costs of transferring those customers. As a result of the enquiries, the AER appoints the following designated RoLRs:

³⁹ s. 132(1) National Energy Retail Law.

⁴⁰ s. 132(2) National Energy Retail Law.

- Victoria: Ozzie Power is appointed the designated RoLR for 10 000 electricity customers and 8 000 gas customers, Dynamic Energy is appointed the designated RoLR for 12 000 electricity customers and Frontier Power is appointed the designated RoLR for 15 000 gas customers.
- South Australia: Magnificent Power is appointed the designated RoLR for 10 000 electricity customers, Focus Energy is appointed the designated RoLR for 8 000 electricity customers and People Power is appointed the designated RoLR for 12 000 gas customers.

The AER considers an appropriate cost recovery scheme would either be an upfront fee, or a retail tariff variation, to recover the transfer costs. The AER considers this appropriate as the RoLRs have agreed to carry the majority of costs. Also, as the RoLR event was due to systemic non-compliance by management and does not threaten the integrity of the energy market, in this context, costs should not be spread over a wider customer base. In this instance it would be appropriate if the customers of the failed retailer bear the costs. A retail tariff variation would be favoured over an upfront fee, if the upfront fee was considered onerous for small customers. The AER notes that the timing of the application and customer composition may be a consideration in deciding whether a retail tariff variation is used to recover costs. The RoLR deemed small customer retail arrangements, over which the AER has the power to vary prices,⁴¹ only last for three months.⁴²

5.3.4 Scenario four

Eternal Energy operates in Queensland, NSW and Victoria, and supplies electricity to 100 000 customers, of which 25 per cent are large customers. Oak Energy is a registered RoLR in NSW with a firm offer for 10 000 large customers and Fundamental Power is a registered RoLR in Queensland with a firm offer for 6 000 large customers.

Eternal Energy is having financial difficulties, due to recent wholesale market volatility increasing its prudential requirements and debts owed to trade creditors and unpaid network charges. Eternal Energy's directors place the company in voluntary administration. This triggers a RoLR event. The AER appoints the following designated RoLRs:

- Queensland: Fundamental Power is appointed the registered RoLR for 5 500 large customers, with the remaining 24 015 customers in Queensland being picked up by the default RoLR for each retail/distribution area.
- NSW: Oak Energy is appointed the registered RoLR for 9 521 large customers, with the remaining 30 479 customers in NSW being picked up by the default RoLR in each distribution area.
- Victoria: The 30 485 customers in Victoria are picked up by the default RoLR for each local retailer area.

⁴¹ s. 145(4) National Energy Retail Law.

⁴² s. 147(3) National Energy Retail Law.

The AER considers an appropriate cost recovery scheme would be for cost recovery to occur through the distributor payment determination levied amongst distributors across the three jurisdictions. Given the size of the failed retailer may lead to significant RoLR scheme costs (i.e. energy purchase costs) being incurred by designated RoLR's, the AER considers the costs of the RoLR event be spread across a wide customer base to minimise the cost impact of the RoLR event on all market participants. The AER may also consider the use of combined upfront free and distributor payment determination to recover RoLR scheme costs.

The AER considers this is supported by the size of the failed retailer, which may mean costs are quite significant, its operation across multiple jurisdictions and the need to minimize the cost impact of a RoLR event on all market participants.

Appendix A—Information from a failing retailer

This appendix sets out the information the AER may seek from a retailer⁴³ to assist it to decide which registered RoLR should be appointed as the designated RoLR. The information requested may vary depending on the circumstances of the failure. Some or all of the information included for guidance below may be included in the request and the information which may be requested is not limited to what is outlined below.

Company structure, contractual arrangements and financial position

1. Information on the current ownership structure of the business.
2. A copy of the retailer's standard contracts.
3. A description of the financial position of the business as at the date of response, with reference to the ability of the business to continue in the immediate future without triggering one or more of the circumstances that are considered to be a RoLR event,⁴⁴ including:
 - a. details of any parent company guarantees
 - b. details of cash flow
 - c. details of amounts owing to distributors
 - d. details of amounts owing to other debtors
 - e. any legal claims which have been made which may affect the business' ability to satisfy the RoLR event criteria in the future
 - f. details of the current financial position including the most recent financial statements of the retailer.

Customer information

4. Total customer numbers split between large and small customers (*example—small or large NMIs*).
5. Total customer numbers split between geographic area (*example—NEM jurisdiction*).
6. Customer load for a specified period split between consumption of large and small customers.

⁴³ In accordance with the AER's powers relating to contingency events under Division 3 of Part 6 of the National Energy Retail Law.

⁴⁴ The circumstances or events that constitute a RoLR event are defined under s 122 of the Retail Law.

Gas arrangements

7. Details of any shippers with whom the business has made contractual arrangements for the shipping of gas.

Appendix B—Registered RoLR tender information

This appendix sets out the information that the AER is likely to request of registered RoLRs under s. 130(5)(a) of the Retail Law if it believes there is a risk of a RoLR event, and there is time before the event to seek the information. The information which may be requested is not limited to what is outlined below.⁴⁵

Customer numbers, tariffs and costs

1. The number of customers for which the business is willing to be appointed as the designated RoLR.
2. For electricity, the class of customers for which the business is willing to be appointed as the designated RoLR.
3. The standing offer terms and conditions including prices which the business would charge electricity and /or gas (as relevant) customers.
4. The terms and conditions including prices which the business would charge electricity and /or gas (as relevant) customers.
5. Whether the business:
 - a. agrees to waive its rights to recover RoLR event costs under a RoLR cost recovery scheme under the Retail Law
 - b. wishes to otherwise vary its RoLR cost recovery scheme under the Retail Law (for example by fixing an amount of costs it can recover).

Energy sourcing arrangements

6. Details of the arrangements the business currently has to source electricity and/or gas (as relevant) to:
 - a. continue supplying existing customers
 - b. supply the customers it has specified it is interested in.

Credit cover arrangements (wholesale market and network)

7. Explanation of how the retailer would be able to meet its credit cover requirements for the customers it has specified an interest in acquiring.
8. If extra credit cover is required, details of how quickly any additional security could be arranged and put in place.

⁴⁵ The AER may provide a standard form for this information to be submitted at the time of a RoLR event.

Glossary

call notice	Has the meaning given by chapter 10 of the National Electricity Rules.
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.
registered RoLR	Has the meaning given in s. 122 of the Retail Law.
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 a first tier retailer failure. Has the meaning given by chapter 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.
