INFORMATION

Recommended changes to retailer of last resort arrangements

The Australian Energy Market Commission (AEMC) has recommended a number of changes to the retailer of last resort (ROLR) arrangements so that they will work more effectively in a broader set of circumstances. These changes are included in the final report of the National Electricity Market (NEM) financial market resilience review.

What are the retailer of last resort arrangements?

If a retailer fails in the NEM, one or more retailers will take responsibility for the failed retailer's customers. These retailers are called the retailers of last resort (ROLRs). ROLR arrangements are designed to quickly transfer customers to a new retailer, so that customers continue to receive retail electricity services without disruption.

These arrangements were reviewed as part of a broader review carried out by the AEMC of the financial resilience of the NEM.

Why are changes to the ROLR arrangements recommended?

If a large retailer fails, the current ROLR arrangements would impose large and immediate financial obligations on ROLRs in the form of increased costs and credit support obligations. If the ROLR is unable to meet its increased obligations very quickly it may be suspended from the NEM. This could trigger a series of retailer failures and threaten the financial stability of the NEM.

For instance, in a scenario where the failed retailer accounts for 20 per cent of NEM market share, high price market conditions exist, and two ROLRs are appointed, it is estimated that the ROLRs would need to organise additional credit support of $672 million to the Australian Energy Market Operator (AEMO); up to $420 million of additional credit support to distribution businesses; and fund an extra $42 million in wholesale market payments each week. The magnitude of such additional financial obligations could cause further retailer failures.

Recommended changes

The AEMC recommends a number of changes to the ROLR arrangements. These changes target the main financial challenges faced by the ROLR if it receives responsibility for a large number of customers because another retailer has failed.

To reduce the impact of the ROLR's increased credit support requirements for its acquired customers, the AEMC recommends:

- waiving for one week the increased credit support that the ROLR must provide to AEMO, and then increasing it over the following four weeks; and
- deferring for five weeks any requirement for the ROLR to provide increased credit support to distribution businesses.

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New retailer of last resort arrangements would work more effectively in a broader set of circumstances and reduce threats to financial stability in the NEM following a retailer failure.

To reduce the impact of the ROLR's increased cash flow requirements, the AEMC recommends:

- giving the ROLR greater certainty that it can quickly recover the reasonable costs of being the ROLR.
- extending the time available for the Australian Energy Regulator (AER) to appoint the ROLR, to increase the potential for the AER to appoint multiple ROLRs. This would spread increased cash flow and credit support requirements across the ROLRs and allow for a more optimal allocation of the failed retailer's customers.
- introducing new arrangements for very large industrial and commercial customers. These changes seek to increase very large customers' awareness of the ROLR scheme and create incentives for them to negotiate their own alternative retailer, which could potentially reduce the size of the ROLR's inherited load and financial obligations. This recommendation is discussed in more detail in a separate information sheet.

Benefits of the recommended changes

The existing ROLR arrangements were designed at a time when there were more medium sized retailers than there are today. The recommended changes would enable the ROLR arrangements to operate more effectively in a broader set of circumstances, including where larger retailers fail, and support continually changing market conditions.

The recommended changes could reduce the financial obligations imposed on the ROLR and would provide more time for those obligations to be met. As a result, financial shocks to the NEM could be absorbed more easily where a retailer fails.

Taken together, these measures may encourage more retailers to offer to become ROLRs, and increase the potential for multiple ROLRs to be appointed. This would reduce the likelihood of further retailer failures and threats to financial stability in the NEM by spreading the customers and financial impacts of ROLR events between several retailers.

Application of the proposed changes

The AEMC's analysis and recommendations have been developed to apply to the ROLR Scheme in the National Energy Customer Framework (NECF). New South Wales, South Australia, Tasmania, and the Australian Capital Territory have already adopted the NECF, and Queensland is scheduled to adopt the NECF on 1 July 2015. In jurisdictions which have not adopted the NECF, the design of the ROLR arrangements is different and these proposed changes would need to be further considered.

Implementation of recommendations

The AEMC has developed its final recommendations for the Council of Australian Governments' (COAG) Energy Council after considering stakeholder views. If the COAG Energy Council accepts the recommendations relating to the ROLR scheme, it would need to develop changes to the National Energy Retail Law and submit rule changes to the AEMC to implement the recommendations.

While the focus of the Commission's advice has been on the NEM, the Commission recommends that the COAG Energy Council also consider applying its recommended changes to the ROLR scheme to gas retailers to provide for a simpler and more comprehensive implementation process. This is because the ROLR scheme in the NECF currently applies the same provisions to both electricity and gas retailer failures.

Background

The recommended changes to the ROLR scheme are part of a number of recommendations proposed by the AEMC to improve the financial resilience of the NEM if an electricity market participant fails. These recommendations are set out in detail in the AEMC's final report for the NEM financial market resilience review, available at www.aemc.gov.au.

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