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Australian Energy Market Commission

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Retailer of Last Resort review – Australian Energy Market Commission

AGL welcomes the opportunity to comment on the Australian Energy Market Commission's (AEMC) review of the Retailer of Last Resort (RoLR) arrangements (the *consultation paper*).

The consultation paper has been informed by the AEMC 2020 Retail Competition review¹ and the impact of COVID-19 on level of consumer energy debt and the AEMC NEM Financial Resilience report completed in 2015 which made a number of recommendations relating to changes in the RoLR arrangements.²

The objective of the RoLR regulatory framework is to ensure energy consumers continue to maintain supply of electricity when their current retailer is no longer able to participate in the provision of retail services due to financial failure. The RoLR is not intended to be the last bastion of a competitive market, nor a required solution for a once in a lifetime global pandemic – it is a pragmatic, simple to understand and implement arrangement backstop for a very unlikely market event. We believe this point should drive any proposed assessment of the success or otherwise of the current RoLR provisions. We also encourage the AEMC to use the experiences and outcomes of previous RoLR events in the sector to make fact based and informed policy options while also taking into account energy market reforms post the NEM Financial Resilience report and how these reforms may impact current RoLR arrangements.

We use the RoLR objective and recent market reforms to assess the AEMC's issues raised in the consultation paper. We recommend maintaining the requirement for RoLR customers to be placed on standard retail contracts. This is based on the view that the AER sets the price for all retailers' standard retail contracts through the Default Mark Offer (DMO). The objective of introducing the DMO was to minimise the adverse price effects the standing offer was seen to have on disengage customers by reviews such as the Australian Competition and Consumer Commission (ACCC) Retail Electricity Pricing Inquiry (REPI) report.³ Hence, it is our view that the standard retail contract with consistent prices across retailers will provide confidence to consumers by ensuring that where a retailer fails, the customer will receive the DMO the AER has deemed a fair and reasonable price for a disengaged customers. This will also be the simplest and least administrative costs approach for industry to manage.

Our key comments on this review are:

¹ <https://www.aemc.gov.au/market-reviews-advice/2020-retail-energy-competition-review>

² <https://www.aemc.gov.au/sites/default/files/content/4d77eb24-c866-4dcd-9d3f-019a61cf417d/NEM-Financial-Market-Resilience-Final-Report-Publication-version.PDF>

³ <https://www.accc.gov.au/regulated-infrastructure/energy/retail-electricity-pricing-inquiry-2017-2018/final-report>



- There is insufficient information and process consideration to support a shift to retailer provided market offers for RoLR customers (e.g. issues with explicit informed consent and administration).
- There are other mechanisms to allow the designation of retailers for RoLR events, including through the Australian Energy Regulator's (**AER**) quarterly reporting process (e.g. scenario planning) that would reduce unnecessary retailer exposure to unhedged amounts.
- Clarifying cost recovery processes (including calculations, time periods) should be a focus area.
- The RoLR obligations should not be shifted to the National Energy Retail Rules (**NERR**) as there is insufficient evidence of such a need (or that there is a failure with the current placement under the National Energy Retail Law (**NERL**)).

Further, we encourage the AER to utilise the existing framework (including the quarterly reporting) to scenario plan and therefore remove the need to delay notification to the market of RoLR customer designation. We provided further comments on these matters in the below attachment.

If you have any questions, please contact Kat Burela on 0498 001 328 or at kburela@agl.com.au.

Regards

Elizabeth Molyneux

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General comments

RoLR arrangements are in place to ensure consumers continue to maintain continuity of electricity supply when their current retailer is unable to meet their financial obligations and therefore cannot continue to provide retail services. As the consultation paper noted, there has been several RoLR events in the NEM and all have smoothly met the objective of the RoLR arrangements.

The AEMC state the current registered RoLRs are limited to the three main retailers for the majority of the NEM and the failure of a number of retailers would therefore reduce competition as the failing retailers' customers would be placed on the three main retailers' standard retail contracts. However, experience from previous retailer failures has shown that a reduction in competition has not eventuated from previous events, and therefore current RoLR arrangements do not lessen competition or create any barriers to entry for new retailers. More recently, standard retail contracts have the same pricing levels for all retailers following the introduction of the DMO.

Importantly, the issue of contagion needs to be considered through a risk-based framework and not through the lens of a 1 in 100-year pandemic event. It is AGL's view the AER Statement of Expectations along with recent changes to the credit management regulatory obligations (for example the new AER hardship guidelines) are the cause of structural changes to the market that have increased the risk of retailer financial viability in the market. Hence, the higher risk of a RoLR is a symptom not the cause of market failure and the AEMC should address the causes as this will provide the least cost and best solution for energy consumers.

Responses to AEMC questions

Standard or Market offers for RoLR customers

While we recognise the intent of the AEMC's proposal to allow retailers to submit market offers for RoLR customers, we believe that the administration of such a process (by both retailer and regulator) is far more complicated than the consultation paper suggest and therefore industry costs of compliance and likely unintended and negative customer impacts outweigh any proposed AEMC benefits.

Standing offers and explicit informed consent

The consultation paper does not explain how retailers and the AER will overcome explicit informed consent (EIC) National Energy Retail Law (NERL) requirements relating to market offers in a RoLR event. While the AEMC suggest the AER will pre-approve retailers' market offers, this does not appear to address NERL EIC obligations. It would not be feasible to get EIC for all RoLR customers prior to designation, so then there would need to be a mechanism to override market offer EIC NERL obligations.

Retailers must keep a record of EIC for market offers, and a range of issues may result through a removal of such a process (e.g. an audit resulting in a number of customers without a record of valid EIC would be a breach of retailer obligations). We do not consider it appropriate for the AEMC to recommend an exception to EIC for market offers in this bespoke way, and instead refer to our submission in February 2020 for the Consumer Protections review on more general EIC reforms.⁴

Default Market Offer vs proposed RoLR market offers

⁴ <https://thehub.agl.com.au/articles/2020/02/agl-encourage-outcomes-focused-regulation-for-consumer-protections>



The DMO was introduced into the electricity market to ensure retailers' standing retail contracts and prices protect dis-engaged customers from financial harm as identified by the REPI Inquiry. Under the DMO all retailers are required to provide their standard contracts at the same DMO price as determined by the AER.

As acknowledged by the AEMC RoLR events are likely to be caused by high price and market costs events in the electricity market. Hence, it is likely that retailers will seek approval of RoLR market offers that are higher priced than generally available market offers. This is to ensure they cover the additional costs associated with RoLR events. Further, retailers will rely on the cost recovery mechanism to recover any difference of their approved RoLR market offer and the actual costs incurred by the RoLR event (see below for further comments on cost recovery mechanism).

Maintaining the RoLR offer as the retailers' standard contract offer will avoid all these additional complexities and costs. Further, under current regulatory arrangements, standard contracts ensure customers maintain continuity of supply at fair, reasonable and consistent terms and conditions, including price, regardless of which retailer is appointed as the RoLR.

Administration issues

There are a range of administrative matters that should be thoroughly considered by the AEMC before a recommendation is made, including:

- **Approval criteria** - needs to be clearly defined and publicly available. These criteria should be consulted on with retailers. For example, how will the AER assess the benefits of a retailer submitted market offer for both the tariffs and non-price terms and conditions mentioned in the AEMC paper?
- **Approval process**
 - should have defined periods for consideration, request for further information and approval (e.g. 2 weeks).
 - Should include an obligation on the AER to provide feedback where they do not accept a retailers' market retail contract. This feedback should also have a defined period to allow retailers to quickly submit an alternative market retail contract for consideration.
- **Changing the market retail contract** – there needs to be a clear process for retailers who wish to update/change their market offer, including what will happen if the AER does not accept an updated version of a retailers market retail contract. For example, if a retailers AER-approved RoLR market retail contract is no longer available in the market and a retailer submits a new plan for approval, what happens if the AER does not approve the subsequent plan? We recommend that the process include:
 - 1) A clear ability for retailers to be able to withdraw a market retail contract for RoLR customers at any time prior to designation.
 - 2) A restriction on the AER's ability to reject a newly submitted market retail contract on the basis of a previously approved market retail contract (e.g. the AER should not be able to reject a new market retail contract simply because the rates have increased since the previous offer was approved).
 - 3) If no other market retail contract has been approved by the AER, those retailers should default to the standard retail contract.
- **Transparency of price and non-price consideration** - the AER's consideration of price and non-price terms and conditions must be transparent. Detail should be provided to the market in regard to how the designation of a RoLR balanced price and non-price terms of all potential RoLR's approved market retail contracts and standard retail contracts.

Maintaining the RoLR offer to the standing offer will also simplify AER cost recovery calculations as we describe further below.



Delaying notification of designation and cost recovery

Delay

The AEMC is proposing to allow the AER to delay the notification of designation by up-to 24 hours to provide time to consider the various retailers that customers may be assigned to. Such a delay would result in the designated RoLR building up liabilities for the failed customers without knowing it. The AEMC state that this risk would be outweighed by the benefits delivered to consumers who may be placed on a better offer.

We do not support the proposal to delay notification of designation due to the risks posed to designated RoLR on built up liabilities for RoLR customers. As we do not support the use of market offers for RoLR events we do not believe this additional time is necessary and the AER can utilise existing arrangements for designation. The AER run a quarterly process where it allows retailers to nominate to be a designated RoLR. As part of this process the AER could run scenarios to determine potential allocation of customers in various zones, reducing the need for a delay in notification.

Should the AEMC pursue a recommendation for allowing a delay, we encourage that this is no greater than 24 hours to help minimise retailer exposure and the costs recovery fully and appropriately compensate RoLR retailers for this risk.

Cost recovery

We support the proposal to introduce greater clarity on RoLR cost recovery arrangements by making clear the types of costs that can be recovered and putting in clear timeframes (e.g. 3 month period, and allowing AER to fast track cost recovery in some cases). It is important that methodologies for AER calculations be transparent to ensure that retailers are not disadvantaged by their exposed hedging position in the initial 24-hour unnotified period (e.g. calculate the recovery for the spot price x load which is consistent with the AEMO settlement process).⁵

However, when combined with the recommendation relating to allowing market offers for RoLR customers, the cost recovery process and calculations become far more complicated.

If the RoLR offer is kept at the standard contract, then it will be easier for the AER to administer the cost recovery process by calculating the DMO costs (which they already have) and the prevailing wholesale conditions during a RoLR event. If the RoLR offer includes different market offers with various price and non-price conditions, the AER will need to reverse calculate against each individual offer to determine cost recovery and will likely increase the evidentiary burden placed on retailers. This is further complicated by each retailer approved RoLR market offer being based on different assumptions of risks and cost by retailers.

Appointment of administrator

We agree with the AEMC's observation that by allowing the appointment of an administrator to trigger a RoLR event, it can cause undue disruption to that retailer's customers should they in fact not fail post-administration. As the AEMC identifies, a company may enter administration if it is facing insolvency, not

⁵ A basic calculation of a hypothetical example where a retailer of 50,000 customers failed during a high price period could result in 9-10 million dollars unhedged exposure in 24 hours.



purely if it is insolvent. It is then the administrator's role to investigate the circumstances of the company and provide a recommendation on how to proceed, which may include:

- selling the company;
- winding up the company; or
- restructuring the company.

It is therefore still possible for a company to trade out of administration and continue trading. In which case, it appears somewhat premature for the appointment of an administrator to trigger a RoLR event and lead to the transfer of customers without further investigation into the circumstances of the appointment and the ability of the company/retailer to successfully trade out of administration.

However, the AEMC's proposal of introducing a "pre-RoLR" event may introduce other issues. This may represent a potential conflict between the administrator's duty to ensure that all (or as many as possible) creditors are repaid and the AER's duty to protect customers. Through the administration process there is often a sale of business or other restructure to "right" the business (the administration allows the administration for example to disclaim uncommercial contracts) which allows it to emerge from administration and continue trading. Administrators are of course minded to retain as much of the revenue stream as is possible in the circumstances, as this will lead to the best post administration outcome (e.g this retains value in the business for any potential sale etc).

This is where confidential discussions between the administrator and the AER as to the retailer's commercial circumstances would be important to ensure that consumers are protected.

Other matters

- **Embedded Networks** – we support the proposal to include embedded network customers in the RoLR arrangements. We note there are currently limitations in the market as not all embedded networks customers and NMI details are visible to the market through AEMO's B2B systems and processes, which may complicate the appointment process.
- **Reference group** – The AEMC paper notes a reference group that has been formed with jurisdictional bodies and the AER as a way to facilitate the legislative changes necessary across each jurisdiction. We encourage the reference group to include industry representation as a part of any discussion regarding the costs and impacts of proposed changes following the AEMC recommendations.
- **NERR to NERL** - we do not support the RoLR scheme requirements moving from the NERL to the NERR as the AEMC has not made a the case for such a change in terms of maintaining or improving consumer protection arrangements with respect to RoLR events. RoLR arrangements are a fundamental protection mechanism and the NERL is the appropriate legislative instrument to house these arrangements and the processes required to seek a change to the NERL are an appropriate mechanism where potential issues with the RoLR scheme are identified and may require changing.