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Australian Energy Market Commission

## **RULE DETERMINATION**

# **NATIONAL ELECTRICITY AMENDMENT (DEFERRAL OF NETWORK CHARGES) RULE 2020**

### **PROPONENT**

Australian Energy Regulator

6 AUGUST 2020

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# **RULE**

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## ABOUT THE AEMC

The AEMC reports to the Council of Australian Governments (COAG) through the COAG Energy Council. We have two functions. We make and amend the national electricity, gas and energy retail rules and conduct independent reviews for the COAG Energy Council.

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## SUMMARY

- 1 On 6 May 2020, the Australian Energy Regulator (AER or proponent) submitted a rule change request to the Australian Energy Market Commission (AEMC or Commission) seeking to amend the National Electricity Rules (NER) to allow electricity retailers to defer the payment of some network charges incurred between 1 July 2020 and 31 December 2020 to distribution network service providers (DNSPs) for six months. The AER's proposal was intended to allow retailers to focus on the ongoing supply of energy as an essential service, and support for customers, as they deal with the cash flow pressures arising as a result of the COVID-19 pandemic. The AER requested that the rule change be expedited as an urgent rule under the NER.
- 2 In response to the rule change proposal, the Commission has made a more preferable rule that introduces a mechanism to allow retailers to defer the payment of some network charges to DNSPs for six months. The more preferable rule applies a number of safeguards in relation to retailer and customer eligibility, the deferral timeframes and the recovery of costs by network service providers (NSPs). In doing so, the final rule balances the need for a framework to provide immediate cash flow relief to retailers to help the market manage the impacts of COVID-19 while ensuring that the impact of the deferral mechanism is manageable and should not pose any material risk for NSPs. This rule change therefore provides a targeted solution that will support the retailers that are most in need during this period.  
**Impact of COVID-19 on the retail electricity market**
- 3 The impacts of, and restrictions associated with, COVID-19 are likely to increase consumer energy debt and in turn reduce retailer revenue. Recent weekly and monthly reports published by the AER, based on information available on 6 July 2020, show a deterioration in some metrics for retail electricity debt in recent months, compared to the second quarter of last year (2019).<sup>1</sup>
- 4 Electricity retailing is a high volume, low margin business. Incremental increases in customer debt may therefore have a significant impact on the financial viability of many retailers, in particular smaller retailers operating in the NEM. The retail margin earned by smaller retailers is considerably lower than that earned by large retailers, meaning that small retailers are likely to be disproportionately impacted by increases in customer debt.
- 5 Feedback provided by participants to this rule change process also suggests that, while the impacts of the pandemic to date appear to have been manageable for most retailers, the full scale of these impacts are still unfolding and are likely to detrimentally impact retailers' cash flows over the next 6 to 12 months.
- 6 In addition to the above issues, the AER's Statement of Expectations<sup>2</sup> notes that it expects

1 As part of the AER Statement of expectations relating to COVID-19, retailers were asked to voluntarily provide customer debt information on a weekly basis.

2 AER, *AER Statement of Expectations of energy businesses: Protecting consumers and the market during COVID-19*, 28 July 2020. Available at: <https://www.aer.gov.au/publications/corporate-documents/aer-statement-of-expectations-of-energy-businesses-protecting-customers-and-the-energy-market-during-covid-19>.

retailers not to disconnect financially vulnerable customers up to (and potentially beyond) 31 October 2020 where that customer has contacted the retailer or is accessing any retailer support. The AER's Statement of Expectations provides important protections to consumers during this period. However, the Commission acknowledges that this increases the risk borne by retailers, as they are expected to continue supplying customers (and incurring the associated supply chain costs) even where a customer has not paid their bill, which creates a potential divergence in cash inflows and outflows.

### Overview of the final rule

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The key features of the more preferable final rule are:

- Some retailers will be able to defer the payment of network charges to DNSPs incurred between 6 August 2020 and 6 February 2021 for eligible customers for six months. There is no provision in this rule to allow for an extension of this timeframe. The deferral timeframes under the final rule are illustrated in the figure below.
- Retailers that are wholly or partly government-owned or registered as a Retailer of Last Resort (RoLR), or a related entity of those retailers, will not be eligible to access these payment deferrals under the final rule.
- Customers for which retailers will be able to defer the payment of network charges include residential and small business customers on a payment plan, hardship arrangement or deferred debt arrangement (collectively referred to as a "COVID-19 customer arrangement" in the final rule) at the time the statement of charges relating to that customer is issued by the DNSP.
- Eligible retailers will be required to:
  - provide a statutory declaration to the DNSP verifying the customers for which a COVID-19 customer arrangement is in place and the amount of network charges payable in respect of those customers
  - pay interest on any deferred network charges at a rate of 3 per cent per annum.
- DNSPs will be able to defer the payment of a proportionate amount of transmission use of system charges to TNSPs, subject to a requirement that the DNSP pass through the corresponding amount of interest earned on deferred network charges to the TNSP. Further, the TNSP is not entitled to charge or recover any other or additional interest in respect of those charges (other than any interest charged under the connection agreement for late payment of TUOS charges).
- Participants are required to negotiate in good faith and agree on processes to give effect to the deferral mechanism under the final rule as soon as practicable, and in any case no later than 10 business days after the commencement date.
- Retailers will be required to report monthly to the AER on the number of customers whose network payments are deferred under the scheme, the total network payments deferred under the scheme and the latest due date for payment of those network charges. The AER will also be required to publicly report on this data each month.
- For the purposes of the credit support rules, the application of the deferral mechanism to any network charges must be taken into account in determining whether any amount is

or remains outstanding, and in determining the time allowed for payment of network charges.

**Figure 1: Deferral timeframes under the final rule**



### Rationale for the final rule

8 The Commission considers that the implementation of a deferral mechanism with the design features discussed above is a necessary and proportionate response to the impacts of COVID-19 on the electricity market. The issues identified above heighten the risk of multiple retailers exiting the market as a direct result of the unique circumstances caused by the COVID-19 pandemic, which do not reflect normal competitive market forces. The Commission considers that multiple retailer failures would not be in the long-term interests of consumers as this would reduce retail competition, which may lead to sub-optimal consumer outcomes. The targeted nature of the deferral mechanism also minimises the impact of the rule change on network businesses by focusing on those retailers that are most in need of support.

9 The final rule addresses this risk while achieving a number of key objectives, including:

- The deferral mechanism under the final rule works in alignment with the AER's Statement of Expectations in that it will allow retailers to continue to support vulnerable customers while managing the inability to disconnect customers for non-payment. This will help address the change to the efficient allocation of risk among market participants which has been a direct result of the COVID-19 pandemic.
- The final rule provides a framework to help manage potential increases in customer non-payment in the second half of 2020 and early 2021. The full economic impacts of COVID-19 on the electricity market, and the economy more broadly, remain unclear in both severity and duration. However, available evidence suggests that these impacts will continue to manifest and potentially worsen over the next six months. The final rule addresses this risk by providing for the deferral of network charges for eligible customers until February 2021. The Commission considers that if further financial support for the retail market is needed beyond this period, including to help retailers manage increased bad debt risk, this may be more appropriately dealt with by alternative policy measures.
- The threat COVID-19 poses to the financial viability of some retailers could have implications for the level of market competition and potential for financial contagion in the NEM. The final rule helps mitigate this risk by providing cash flow relief to those retailers that are more likely to be in financial distress, thereby giving those retailers the

opportunity to adjust their operations as required to respond to the pandemic and reducing the likelihood of those retailers exiting the market in the short term.

- The deferral mechanism under the final rule incorporates a number of limitations compared to the AER's proposal. This will allow the impacts of COVID-19 to be shared across parts of the electricity supply chain without imposing an overly detrimental financial burden on network businesses. The final rule also imposes incentives on retailers to manage their cash flow risk by requiring interest to be paid on any deferred charges.

10 The Commission published a directions paper and proposed rule drafting on 9 July 2020 to undertake additional consultation on the implementation of the deferral mechanism. The final rule incorporates feedback provided by stakeholders in response to the directions paper to ensure the mechanism can be implemented effectively, including making changes to the rules drafting to:

- clarify the retailer and customer eligibility requirements
- clarify the treatment of interest on deferred charges where a retailer becomes insolvent
- prescribe an appropriate timeframe (10 business days) in which participants must implement processes to give effect to the final rule.

11 The Commission notes that the policy design choices under the final rule have been informed by the extraordinary circumstances associated with COVID-19 and the need to have a framework in place as quickly as possible to assist the market in dealing with the impacts of the pandemic. This rule change was assessed on an urgent basis in order to achieve this objective and the approach to determining eligibility criteria and implementation processes should therefore not be interpreted as setting a precedent for future decisions.

## CONTENTS

<b>1</b>	<b>AER's rule change request</b>	<b>1</b>
1.1	The rule change request	1
1.2	Context	1
1.3	Issues raised in the AER's rule change request	3
1.4	Solution proposed in the rule change request	4
1.5	The rule making process	5
<b>2</b>	<b>Why a deferral mechanism is needed</b>	<b>7</b>
2.1	Overview	7
2.2	Proponent's views	7
2.3	Stakeholder views	8
2.4	Commission's analysis	8
<b>3</b>	<b>Final rule determination</b>	<b>12</b>
3.1	The Commission's final rule determination	12
3.2	Rule making test	12
3.3	Assessment framework	13
3.4	Summary of reasons	14
3.5	Implementation	17
	<b>Abbreviations</b>	<b>18</b>

## APPENDICES

<b>A</b>	<b>Legal requirements under the NEL</b>	<b>19</b>
A.1	Final rule determination	19
A.2	Power to make the rule	19
A.3	Commission's considerations	19
A.4	Civil penalties	20
A.5	Conduct provisions	20
<b>B</b>	<b>Retailer eligibility and incentives</b>	<b>21</b>
B.1	Overview	21
B.2	Proponent's views	21
B.3	Stakeholder views	22
B.4	Commission's analysis and conclusions	24
<b>C</b>	<b>Customer eligibili</b>	<b>29</b>
C.1	Overview	29
C.2	Proponent's views	29
C.3	Stakeholder views	29
C.4	Commission's analysis and conclusions	30
<b>D</b>	<b>Deferral timeframe and terms</b>	<b>32</b>
D.1	Overview	32
D.2	Proponent's views	32
D.3	Stakeholder comments	32
D.4	Commission's analysis and conclusions	34
<b>E</b>	<b>Deferral of payments between DNSPs and TNSPs</b>	<b>37</b>
E.1	Overview	37

E.2	Proponent's views	37
E.	Stakeholder views	37
E.4	Commission's analysis and conclusions	37
<b>F</b>	<b>Practical implementation of payment deferrals</b>	<b>39</b>
F.1	Overview	39
F.2	Proponent's views	39
F.3	Stakeholder views	39
F.4	Commission's analysis and conclusions	40
<b>G</b>	<b>Reporting requirements</b>	<b>42</b>
G.1	Overview	42
G.2	Proponent's views	42
G.3	Stakeholder views	42
G.4	Commission's analysis and conclusions	43
<b>H</b>	<b>Impact on NSPs</b>	<b>44</b>
H.1	Overview	44
H.2	Proponent's views	44
H.3	Stakeholder views	44
H.4	Commission's analysis and conclusions	45
<b>I</b>	<b>Summary of other issues raised in submissions</b>	<b>48</b>

## TABLES

Table 2.1:	AER scenario modelling of impact of COVID-19 on retailers	7
Table B.1:	Variable business lending rates for new loans funded in the month (per annum)	26
Table H.1:	Estimated impact of deferral mechanism on representative NSW DNSP's annual revenue	46
Table I.1:	Summary of other issues raised in submissions to consultation paper	48

## FIGURES

Figure 1:	Deferral timeframes under the final rule	iii
Figure 2.1:	Illustrative impact of COVID-19 on EBITDA	10
Figure D.1:	Deferral timeframes under final rule	36



# 1 AER'S RULE CHANGE REQUEST

This chapter discusses the details of:

- the AER's rule change request
- the market context given the impacts of COVID-19
- the issues identified by the AER
- the solution proposed by the AER
- the rule making process.

## 1.1 The rule change request

On 6 May 2020, the Australian Energy Regulator (AER or proponent) submitted a rule change request to the Australian Energy Market Commission (AEMC or Commission) seeking to amend the National Electricity Rules (NER) to allow electricity retailers to defer the payment of some network charges incurred between 1 July 2020 and 31 December 2020 to distribution network service providers (DNSPs) for six months. The AER's proposal was intended to allow retailers to focus on the ongoing supply of energy as an essential service, and support for customers, as they deal with the cash flow pressures arising as a result of the COVID-19 pandemic.

## 1.2 Context

The COVID-19 pandemic has severely disrupted economic activity across Australia. This section summarises some of the key impacts of COVID-19 which have the potential to significantly affect the electricity market.

### 1.2.1 Residential customers

Millions of Australians' incomes have been affected by job losses, pay reductions or reduced work hours. This is partially reflected in the unemployment rate, which has increased from 5.2 per cent at the beginning of March 2020 to 7.4 per cent in June 2020.<sup>3</sup> However, the Federal Government has recently stated that the effective unemployment rate is 11.3 per cent when those who have left the workforce or those who are on zero hours are taken into account. Some institutions have also forecast unemployment to rise higher. For example, the Grattan Institute estimated the unemployment rate could rise to between 10 and 15 per cent.<sup>4</sup> The variation in these estimates underlines the uncertainty of estimating the economic and employment impact of the crisis.

For those who remain in employment, incomes are also being impacted by the pandemic. A study by Monash University noted that prior to the pandemic 81 per cent of people surveyed reported an average weekly income of \$500 or more. Following the start of the pandemic,

<sup>3</sup> Australian Bureau of Statistics, *6202.0 - Labour Force, Australia, Jun 2020*, 16 July 2020, available at: <https://www.abs.gov.au/ausstats/abs@.nsf/mf/6202.0>.

<sup>4</sup> Grattan Institute, *Shutdown: estimating the COVID-19 employment shock*, April 2020, p. 3.

the same people reported large drops in their income, with just under 29 per cent reporting more than \$500 of weekly income.<sup>5</sup>

Despite the assistance provided by a number of government income and payment assistance support measures, many households that were previously on full time employment may experience financial hardship for the foreseeable future through increased job insecurity, difficulty finding new jobs and reduced income. This income reduction and increased sense of insecurity may influence a consumer's ability and willingness to pay energy bills.

### 1.2.2 Small business customers

Small business consumers have also been significantly affected by the pandemic and the associated social distancing restrictions imposed by governments. Data published by the Australian Bureau of Statistics (ABS) in June showed that two-thirds of businesses surveyed reported a decrease in revenue compared to last year, with almost one in three of those businesses reporting a decrease of 50 per cent or more.<sup>6</sup> While wages for certain employees are covered by the JobKeeper allowance, businesses must also consider a range of overhead costs such as servicing loan payments, payments associated with utilities, insurance, rent and equipment. In recognition of these challenges, the members of the Australian Banking Association announced a loan repayment deferral of up to six months for affected small businesses.

### 1.2.3 Changes in energy demand

Data provided by Victorian DNSPs shows that overall energy demand throughout the pandemic has decreased by approximately two per cent compared to the previous year.<sup>7</sup> The changes in energy demand can be broken down by customer segment:

- overall business consumption in Q2 2020 was about 10 to 15 per cent lower on average than the same period last year
- small business consumption in April 2020 was about 30 per cent lower on average than the same period last year
- residential consumption in Q2 2020 was about 20 per cent higher on average than the same period last year.

The increase in residential demand is attributed to government policies aimed at minimising social interaction by requiring consumers to remain at home, as well as the increased number of people working from home on a daily basis. Similarly, restrictions to non-essential businesses such as cafes and restaurants have likely contributed to the reduction in small business demand.

5 Monash University, *Monash COVID-19 health and work study*, April 28 2020, available at <https://theconversation.com/90-out-of-work-with-one-weeks-notice-these-8-charts-show-the-unemployment-impacts-of-coronavirus-in-australia-136946>

6 ABS, 5676.0.55.003 - *Business Indicators, Business Impacts of COVID-19*, June 2020, available at: <https://www.abs.gov.au/AUSSTATS/abs@.nsf/Latestproducts/5676.0.55.003Main%20Features1June%202020?opendocument&tabname=Summary&prodno=5676.0.55.003&issue=June%202020&num=&view=>

7 ENA, Mapping the impact of COVID-19 on electricity demand, 16 July 2020, available at: <https://www.energynetworks.com.au/news/energy-insider/2020-energy-insider/mapping-the-impact-of-covid-19-on-electricity-demand/>.

While the full impact of restrictions is unlikely to be clear in the short-term, increased residential energy usage will likely lead to an increase in residential energy bills. The Public Interest Advocacy Centre has estimated that bills may increase by \$200 a month during winter months for certain consumers.<sup>8</sup>

### 1.3 Issues raised in the AER's rule change request

The AER's rule change request noted that many electricity customers in the NEM are facing difficulties paying their bills as a result of the economic impacts of the COVID-19 pandemic, with over 20,000 electricity customers registering for payment plans since early March 2020 and over a thousand customers per week currently seeking assistance from retailers. The AER considered that the COVID-19 pandemic could potentially lead to multiple retailer failures and thereby undermine the operation of retail electricity markets. This is due to the financial pressures on retailers resulting from the potential divergence between their incoming cash flows from customers affected by the pandemic and their outgoing cash flows required to satisfy their obligations to pay wholesale and network energy charges.

The AER noted that, at the time of its rule change request, its Statement of Expectations of energy businesses outlined the support the AER expected energy retailers to provide to customers during the COVID-19 pandemic, including that retailers not disconnect customers who may be in financial stress for non-payment of their electricity bills before 31 July 2020 and potentially beyond.<sup>9</sup> This arrangement meant that retailers took on the risk of incurring ongoing network and wholesale energy costs without matching revenue streams to meet those costs.

The AER also considered that the Retailer of Last Resort (RoLR) mechanism, which provides for customers to transfer to another retailer in the event of retailer failure, may not be capable of mitigating the risk of multiple retailers failing as a result of COVID-19 induced financial pressures.

The Electricity and Gas Network Relief Package (Network Relief Package) established by network businesses in New South Wales, Victoria and South Australia was designed to provide some financial relief to customers (and, by extension, retailers) enduring hardship as a result of COVID-19.<sup>10</sup> The Network Relief Package provided for:

- the deferral of network charges incurred from 1 April 2020 to 30 June 2020 for residential customers of certain large retailers<sup>11</sup> who are put on a payment plan or hardship arrangement as a result of the pandemic
- rebates for network charges incurred from 1 April 2020 to 30 June 2020 for:

<sup>8</sup> PIAC, *Community and consumer organisation joint proposal: National COVID-19 energy hardship relief package*, March 2020, available at: <https://piac.asn.au/wp-content/uploads/2020/03/COVID-19-National-Energy-Hardship-Relief-Package.pdf>.

<sup>9</sup> The AER published an updated version of its Statement of Expectations on 28 July 2020. This version of the Statement of Expectations requires retailers to not disconnect customers that may be financially vulnerable before 31 October 2020 (and potentially beyond) where the relevant customer has contacted the retailer or is receiving any retailer support.

<sup>10</sup> For more information, see <https://www.energynetworks.com.au/news/media-releases/2020-media-releases/energy-network-relief-package-announced/>.

<sup>11</sup> Customers of AGL Energy, EnergyAustralia, ERM Power, Lumo Energy, Momentum Energy, Origin Energy, Red Energy and Simply Energy may be eligible for the deferral.

- residential customers of small retailers that "go into default" as a result of the pandemic
- small business customers of all retailers that use less than 25% of historical average consumption for that period.

The rebates are to be provided to retailers by the end of September 2020.

The Network Relief Package was implemented on a jurisdictional basis following consultation between NSPs and retailers. In the AER's view, the economic impacts of COVID-19 and the associated impact on retailers' revenue streams will continue to manifest throughout the second half of 2020. The AER therefore considered it necessary that the financial support provided by the Network Relief Package be extended beyond June 2020 in the form of the proposed deferral mechanism. The Commission notes that, in practice, the relief provided to retailers by the Network Relief Package did not cease to have effect on 30 June 2020. This is discussed further in appendix d.

## 1.4

## Solution proposed in the rule change request

### 1.4.1

### Deferral of payment of network charges by retailers

The AER's rule change request proposed that the NER be amended to provide for the payment of some network charges by retailers incurred between 1 July 2020 and 31 December 2020 to be deferred for an initial period of six months. This deferral would only apply to network charges incurred in relation to customers on a "COVID-19 customer arrangement" during this period. This would capture any customer who, between 1 March 2020 and 31 December 2020, entered into:

- a payment plan<sup>12</sup>
- any arrangement as a hardship customer<sup>13</sup>
- any deferred debt arrangement.<sup>14</sup>

The deferral mechanism would not apply to customers who became hardship customers or were on a payment plan or deferred debt arrangement prior to 1 March 2020.

Under the AER's proposal, all retailers would be able to defer the payment of network charges for eligible customers. However, the AER suggested that the Commission consider whether only certain retailers should be eligible to access this support and, if so, how this should be determined. This issue is discussed further in appendix b.

The AER noted that retailers would still be responsible for managing the risk of customer default and NSPs would remain entitled to recover the full amount of their regulated revenues as determined by the AER. The AER identified some options under the existing

<sup>12</sup> The NERL defines "payment plan" as a plan for a hardship customer, or a residential customer who is not a hardship customer but who is experiencing payment difficulties, to pay a retailer, by periodic instalments in accordance with the Rules, any amounts payable by the customer for the sale and supply of energy.

<sup>13</sup> The NERL defines "hardship customer" as a residential customer of a retailer who is identified as a customer experiencing financial payment difficulties due to hardship in accordance with the retailer's customer hardship policy.

<sup>14</sup> The AER's proposal defines "deferred debt arrangement" as any arrangement by which the payment of a debt owed or expected to be owed by a shared customer to a retailer for the supply of energy is deferred.

regulatory framework which may allow networks to recover the efficient costs they may incur as a result of the proposed deferral mechanism, including:

- charging retailers interest on the deferred payments at the default interest rate
- passing the costs through to network customers under existing cost pass through mechanisms (although the AER notes the threshold for these mechanisms may not be exceeded unless the impact on retailers is sustained and severe).

#### 1.4.2

##### Deferral timeframe

As discussed above, the AER's proposal would allow the payment of some network charges to be deferred by six months. At the end of the deferral period, the retailer would be required to pay the deferred network charges regardless of whether the retailer has been paid by the relevant customer. Given that the payment deferral could relate to network charges incurred up to 31 December 2020, the effects of the proposed rule would conclude six months after the invoicing of network charges for the October to December quarter of 2020, which is expected to be between July and August 2021 (subject to extension by the AER as discussed below).

The AER also proposed that it be given the power under the rules to extend the deferral period beyond 31 December 2020 if the AER considers it reasonably necessary to do so. This issue is discussed further in appendix d.

#### 1.4.3

##### Rule making process and commencement

As discussed in section 1.3, this rule change request is seeking to address the unprecedented circumstances presented by COVID-19 and the significant financial risks the current economic environment poses for electricity retailers. On that basis, the AER requested that the Commission treat the rule change proposal as an urgent rule under the NEL. The AER proposed that the rule commence on 1 July 2020 so that it would apply to statements of charges issued by NSPs to retailers from that date until 31 December 2020. The process for this rule change, including the treatment of the rule change as urgent, is discussed further in section 1.5.

### 1.5

## The rule making process

On 28 May 2020, the Commission published a notice advising of its commencement of the rule making process and consultation in respect of the rule change request.<sup>15</sup> A consultation paper identifying specific issues for consultation was also published. The Commission held a briefing for all interested stakeholders on 1 June 2020 to provide an overview of the consultation paper and explain the rule change process.

The Commission accepted that the rule change request was a request for an urgent rule as defined in s. 96 of the NEL. Accordingly, the Commission commenced an expedited rule change process, subject to any written requests not to do so. The closing date for receipt of written requests was 11 June 2020. No requests to not carry out an expedited rule change

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<sup>15</sup> This notice was published under s. 95 of the National Electricity Law (NEL).

process were received. Accordingly, the rule change request was considered under an expedited process.<sup>16</sup>

Submissions to the consultation paper closed on 25 June 2020. The Commission received 26 public submissions, as well as a number of confidential submissions. Issues raised in public submissions that are not discussed in the body of this document have been summarised and responded to in appendix i.

On 7 July 2020, the Commission extended the period of time for making the final determination for the rule change request from 23 July 2020 to 6 August 2020 under section 107 of the NEL. The Commission considered that this extension was necessary due to the complexity of the issues raised in the rule change request and submissions to the consultation paper. In particular, the Commission considered it necessary to test the proposed changes to the rules required to give effect to the deferral mechanism with stakeholders. Several stakeholders also requested that additional time be allowed for consideration of these issues and further consultation.

This extension allowed the Commission to publish a directions paper on 9 July 2020 to facilitate further stakeholder consultation on the proposed rule change. The directions paper flagged the Commission's intention to introduce a deferral mechanism under the final rule and set out the Commission's proposed policy positions in respect of the design of the mechanism. The Commission also published indicative rule drafting to give effect to the policy positions outlined in the directions paper. The Commission sought stakeholder feedback on the proposed rule drafting, particularly whether it would allow the deferral mechanism to be implemented in an effective and timely manner. Submissions were due by close of business on 23 July 2020. The Commission received a number of submissions from network businesses, consumer representatives and retailers, some of which provided specific feedback on various implementation issues in the proposed rule drafting. This feedback has been taken into consideration in the Commission's development of the final rule.

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<sup>16</sup> Section 96 of the NEL.

## 2 WHY A DEFERRAL MECHANISM IS NEEDED

### 2.1 Overview

One of the major concerns raised by the AER in its rule change request related to the impact of the COVID-19 pandemic on industry costs and capacity, and the extent to which that may impact the financial resilience of the NEM and its participants, and the secure and reliable operation of the NEM. The Commission sought feedback from retailers in the consultation paper on the materiality and expected duration of the impacts of COVID-19 on their cash flows, as well as whether existing support measures were adequately addressing these issues.

This section sets out stakeholders' views on the impacts of COVID-19 on retailers and the Commission's analysis of this issue.

### 2.2 Proponent's views

The AER undertook scenario modelling of the possible electricity retail sector impacts of COVID-19 and provided the results in its submission to the consultation paper. These results are summarised in the table below.

**Table 2.1: AER scenario modelling of impact of COVID-19 on retailers**

SCENARIO	REDUCTION IN RETAILER REV- ENUE	CUMULATIVE NEGATIVE CASH FLOW TO RETAILERS OVER 6 MONTHS
Low impact scenario	Residential customers: 5% Small business customers: 5% C&I customers: 2%	\$270M
Medium impact scenario	Residential customers: 10% Small business customers: 10% C&I customers: 5%	\$844M

Source: AER, submission to consultation paper, p. 2.

The AER noted that it did not seek to estimate the impacts on, including the solvency of, specific retailers. Its modelling also does not account for:

- existing debt levels, or the cash reserves held by retailers or, where relevant, their parent companies
- the ability of individual retail businesses to source credit.



The AER considered this modelling illustrates the scale of the issue facing Australia's electricity sector and demonstrates the prudence of regulatory intervention to mitigate the risk of multiple, cascading, retailer failures.<sup>17</sup>

## 2.3 Stakeholder views

Most stakeholders commented in submissions to the consultation paper on the observable impact to date of COVID-19 on the retail electricity market, and the implications for the design of the proposed deferral mechanism. Relevant comments are summarised below.

Retailers provided information on the impacts of COVID-19 they have observed to date, with many noting that some elements of these impacts are difficult to quantify at this point in time but are expected to worsen in the coming months.<sup>18</sup> This has included changes in customer payment behaviour, including increasing instances of late payment and bad debt, and increases in the number of customers seeking support and entering into deferred payment arrangements with retailers. Some retailers also made confidential submissions providing further details of the impacts on their business to date. Many retailers expressed concern that customer payment issues are likely to materially increase in the second half of 2020 once existing financial support schemes which are currently helping customers pay their bills expire.

Network businesses that commented on this issue generally considered that the evidence available to date does not demonstrate a need to provide urgent financial relief to retailers, or an imminent risk of cascading retailer failures.<sup>19</sup> Some networks suggested that a range of other COVID-19-related measures already put in place to support energy customers and retailers are sufficient to address any cash flow issues retailers may be facing. It was also suggested that retailers exiting the market is a natural outcome of a competitive retail market.

## 2.4 Commission's analysis

COVID-19 restrictions and impacts are likely to increase consumer energy debt and in turn reduce retailer revenue. Recent weekly and monthly reports published by the AER, based on information available on 6 July 2020, show a deterioration in some, but not all, metrics for retail electricity debt in recent months, compared to the second quarter of last year (2019).<sup>20</sup>

- **Residential electricity customers**<sup>21</sup>
  - Between Q2 2019/20 and 6 July 2020, the average proportion of electricity customers with debt to repay increased by 0.76 per cent to 3.36 per cent, while the average amount of debt increased by 31.5 per cent to \$945.51.

<sup>17</sup> AER, submission to consultation paper, p. 2.

<sup>18</sup> See for example, submissions to consultation paper: AGL, p. 2; EnergyAustralia, p. 6; Locality Planning Energy, p. 2; Next Business Energy, p. 3; Origin Energy, p. 2; Simply Energy, p. 2.

<sup>19</sup> See for example, submissions to consultation paper: Ausgrid, p. 5; ENA, p. 7; TransGrid, p. 6.

<sup>20</sup> As part of the AER Statement of expectations relating to COVID-19, retailers were asked to voluntarily provide customer debt information on a weekly basis.

<sup>21</sup> AER, *Retail market data dashboard - 6 July 2020 - COVID-19*, p. 1.



- Between 30 March 2020 and 6 July 2020, the average proportion of electricity customers with debt to repay increased by 0.12 per cent to 3.36 per cent and the average amount of debt per customer increased by 18.15 per cent to \$945.51.
- **Small business customers<sup>22</sup>**
  - Between Q2 2019/20 and 6 July 2020, the average proportion of electricity customers with debt to repay increased by 2.43 per cent to 4.2 per cent, while the average amount of debt increased by 8.98 per cent to \$2,212.79.
  - Between 30 March 2020 and 6 July 2020, the average amount of debt per customer decreased by 3.15 per cent to \$2,212.79 and the average proportion of customers repaying debt increased by 1.44 per cent to 4.2 per cent.
- **Electricity hardship programs<sup>23</sup>**
  - Between Q2 2019/20 and 6 July 2020, the average proportion of electricity customers on hardship programs increased by 0.08 per cent to 1.17 per cent, while the average hardship debt decreased by 0.17 per cent to \$1,403.42.
  - Between 30 March 2020 and 6 July 2020, the average amount of debt per electricity hardship customer increased by 10.12 per cent to \$1,403.42 and the average proportion of customers on a hardship program increased by 0.03 per cent to 1.17 per cent.
- **Payment plans**
  - The AER noted that the number of customers on payment plans was slightly lower in Q2 2020, compared to Q2 2019. This may reflect that many retailers were offering customers the option to defer outstanding arrears payments, typically until 31 July. These payment deferrals and extensions are not included in the AER's data, as they are not captured under the AER's definition of a payment plan.<sup>24</sup>

In relation to the above AER data, the Commission notes:

- The data has a significant time lag, and may not be an accurate reflection of current or future debt levels. Most small customers pay for their electricity consumption quarterly in arrears, which creates a natural lag between broader economic conditions, and the cash position of retailers. Additionally, there is a further time-lag from a customer missing a payment, to it entering a hardship program, and the debt being categorised as bad debt.
- The data is based on information provided by most, but not all, electricity retailers.
- Deferrals and extensions offered by retailers to customers, typically until 31 July 2020, are not captured under the AER's definition of a payment plan. This means the AER's reporting may be materially understating the increase in the number and proportion of customers in debt.

Increased customer debt may have a significant impact on the financial viability of many retailers, in particular smaller retailers operating in the NEM. In December 2019, the ACCC reported that retailers in the NEM have an average retail margin or earnings before interest,

<sup>22</sup> AER, *Retail market data dashboard - 6 July 2020 - COVID-19*, p. 1.

<sup>23</sup> AER, *Retail market data dashboard - 6 July 2020 - COVID-19*, p. 2.

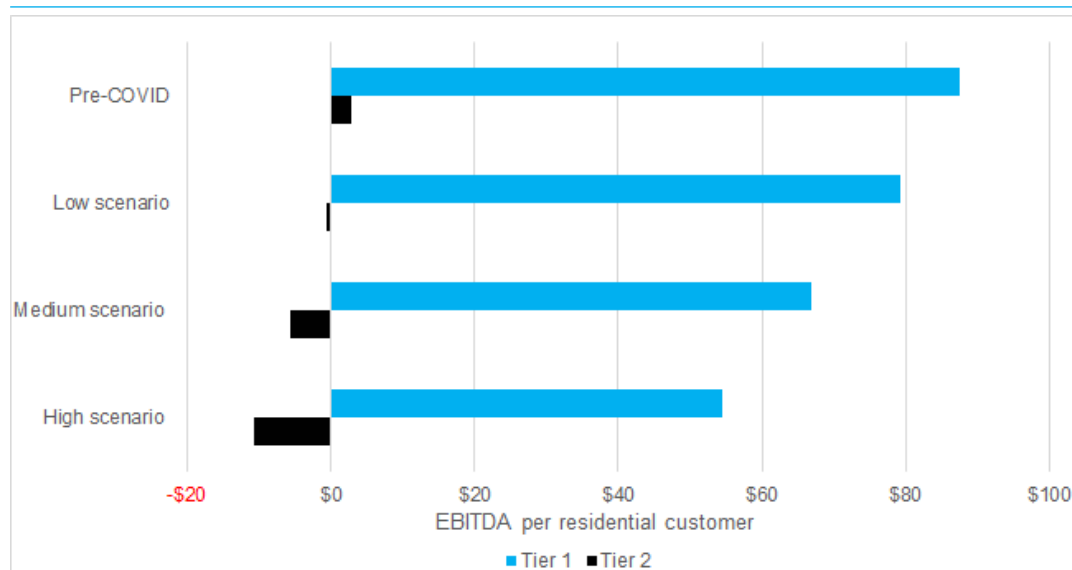
<sup>24</sup> AER, *Retail market data dashboard - 6 July 2020 - COVID-19*, p. 1.

tax, depreciation and amortisation (EBITDA) of around four per cent, or \$60, per residential customer.<sup>25</sup> However, this retail margin is estimated to be considerably less for smaller retailers. The AEMC's 2020 Retail Energy Competition Review presented an illustrative scenario analysis exploring the impact of increased debt on retailer margins. The illustrative example explored three scenarios, including:

- low scenario — representing a 200 per cent increase in hardship and debt collection costs
- medium scenario — representing a 350 per cent increase in hardship and debt collection costs
- high scenario — representing a 500 per cent increase in hardship and debt collection costs.<sup>26</sup>

The results from the analysis are presented in Figure 2.1 below.

**Figure 2.1: Illustrative impact of COVID-19 on EBITDA**



Source: AEMC analysis of ACCC data

Note: The results presented are illustrative, and are reliant on numerous assumptions, including: all bill stack components, aside from retail costs, are the same between Tier 1 and 2 retailers; 'other retail costs' are the same across Tier 1 and 2 retailers; hardship and debt collection costs increase at the same rate, whilst other retail costs do not change.

While the scenario analysis results in Figure 2.1 are illustrative, and based on a number of assumptions, they indicate that small retailers are likely to be disproportionately impacted by increasing debt. Additionally, this analysis does not account for recent changes to consumption profiles due to COVID-19. For example, because of the lock down restrictions small business consumption has fallen while residential consumption has increased. Retailers

<sup>25</sup> ACCC, *Inquiry into the National Electricity Market* - November 2019, p. 6.

<sup>26</sup> AEMC, 2020 Retail energy competition review, Final report, 30 June 2020, p. 145.

generally have a greater margin on small business consumers, and as such their total margin and revenue is likely to have fallen.<sup>27</sup>

The Retail Energy Competition Review also identified four factors that are likely to impact a retailer's financial resilience in the face of COVID-19, including its profitability before the pandemic, its corporate and financial structure, its hedging strategy and its customer service and IT locations.<sup>28</sup> The Commission stated that it is likely a combination of all these factors would impact a retailer's ability to stay solvent in light of the full economic impact of COVID-19, as the impact of the pandemic has the potential to vary considerably between retailers.

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27 The ACCC reported that NEM average retail margins for residential consumers is 1.3 c/kWh, while the average retail margin for small businesses is 2.3 c/kWh. For more information see: <https://www.accc.gov.au/publications/inquiry-into-the-national-electricity-market-november-2019-report>.

28 AEMC, *2020 Retail energy competition review*, Final report, 30 June 2020, pp. 141-148.

## 3 FINAL RULE DETERMINATION

### 3.1 The Commission's final rule determination

The Commission's final rule determination is to make a more preferable final rule to allow certain retailers to defer the payment of network charges incurred in respect of certain customers between 6 August 2020 and 6 February 2021 to DNSPs for six months. While the final rule adopts some elements of the AER's proposal, it also includes additional safeguards to ensure that:

- the scope of the deferral mechanism is narrowed by imposing appropriate entry criteria (i.e. excluding RoLR retailers and government-owned retailers, and their related entities) and incentives on retailers, while still allowing payment deferrals to be administered in a timely manner
- eligible retailers can only defer the payment of network charges for residential and small business customers on a payment plan, hardship arrangement or deferred debt arrangement
- retailers will be required to pay interest on deferred network charges in order to allow NSPs to recover the efficient costs they may incur as a result of the payment deferrals
- where a retailer defers the payment of network charges to a DNSP, the DNSP can also defer the payment of the relevant transmission use of system (TUOS) charges to the transmission network service provider (TNSP).

The proposed design of the deferral mechanism is discussed in more detail in the appendices.

The Commission's reasons for making this final rule determination are set out in section 3.4.

Further information on the legal requirements for making this final rule determination is set out in appendix a.

### 3.2 Rule making test

#### 3.2.1 Achieving the NEO

Under the NEL the Commission may only make a rule if it is satisfied that the rule will, or is likely to, contribute to the achievement of the national electricity objective (NEO).<sup>29</sup> This is the decision making framework that the Commission must apply.

The NEO is:<sup>30</sup>

to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to:

- (a) price, quality, safety, reliability and security of supply of electricity; and
- (b) the reliability, safety and security of the national electricity system.

<sup>29</sup> Section 88 of the NEL.

<sup>30</sup> Section 7 of the NEL.

### 3.2.2 Making a more preferable rule

Under s. 91A of the NEL, the Commission may make a rule that is different, including materially different to a proposed rule (a more preferable rule) if it is satisfied that, having regard to the issue or issues raised in the rule change request, the more preferable rule will or is likely to better contribute to the achievement of the NEO.

In this instance, the Commission has made a more preferable rule. The reasons for making a more preferable rule are discussed in section 3.4.

### 3.2.3 Making a differential rule

Under the Northern Territory legislation adopting the NEL, the Commission may make a differential rule if, having regard to any relevant MCE statement of policy principles, a different rule will, or is likely to, better contribute to the achievement of the NEO than a uniform rule. A differential rule is a rule that:

- varies in its term as between:
  - the national electricity system, and
  - one or more, or all, of the local electricity systems, or
- does not have effect with respect to one or more of those systems

but is not a jurisdictional derogation, participant derogation or rule that has effect with respect to an adoptive jurisdiction for the purpose of s. 91(8) of the NEL.

As the rule relates to parts of the NER that currently do not apply in the Northern Territory, the Commission has not assessed the rule against the additional elements required by the Northern Territory legislation.<sup>31</sup>

## 3.3 Assessment framework

In assessing the rule change request against the NEO the Commission has considered the following principles:

- **Promoting financial resilience** — whether the rule change proposal would support industry viability and financial resilience by deferring costs for retailers facing cash flow risks as a result of the COVID-19 pandemic. This could therefore reduce the potential for multiple retailer failures and financial contagion attributable to the impact of COVID-19. The support provided by this financial relief may also support the continuation of a competitive market structure, which in turn will support better pricing outcomes for consumers.
- **Efficient allocation of risk** — whether the rule change proposal would appropriately allocate any associated risk and cost to the parties best placed to manage them. This involved consideration of the risk profiles of different market participants, including businesses within the same participant class, and the implications for the design of the

<sup>31</sup> From 1 July 2016, the NER, as amended from time to time, apply in the NT, subject to derogations set out in regulations made under the NT legislation adopting the NEL. Under those regulations, only certain parts of the NER have been adopted in the NT. (See the AEMC website for the NER that applies in the NT.) National Electricity (Northern Territory) (National Uniform Legislation) Act 2015.

proposed deferral mechanism. The rationale for the allocation of risk under existing regulatory arrangements is discussed in Box 1.

- **Implementation costs** — where costs are imposed in implementation and cannot be mitigated through market mechanisms, these costs should be minimised relative to the benefits of the proposed deferral mechanism.

#### BOX 1: RISK ALLOCATION IN THE NEM

Electricity retailers carry the credit and cash-flow risks for the entire electricity supply chain. Notably, retailers are required to make payments for non-retail supply chain components, including network charges, by defined time frames regardless of the level of non or late-payment by customers.

The Commission considers that risks should generally rest with the participants that are best placed to manage them. As the participant with direct relationships with customers, retailers are best placed to manage the risk of non or late-payment by customers. For example, for small consumers retailers have developed strategies such as pay on time discounts, late payment fees and advanced payments to manage late payment risks. For large consumers, retailers are able to negotiate terms within their contracts to ensure timely payment (for example, credit support). Retailers may also build in the cost of late or non-payment into their prices. Retailers bearing this risk therefore generally represents an efficient allocation of risk within the sector.

As suppliers of essential services, energy retailers enter the NEM with knowledge that they are required to continue to supply small customers who do not pay, or pay late, to a greater degree than retailers of most products and services in the economy. These requirements are set out within the hardship and disconnection regulations in the National Energy Retail Law (NERL) and National Energy Retail Rules (NERR). Where retailers are not able to withstand increases in the level of non or late-payment, the Commission generally considers these retailers will exit the market and this a feature of the competitive process.

However, the unprecedented circumstances presented by the COVID-19 pandemic may justify providing assistance to retailers to manage cash flow risks that are exceptions to the usual efficient allocation of cash-flow risk within the sector. In particular, the AER's Statement of Expectations of energy businesses expects retailers to continue to supply non-paying customers to a greater degree than could have been foreseen by retailers before the crisis.

## 3.4 Summary of reasons

The more preferable final rule made by the Commission is attached to and published with this final rule determination.

### 3.4.1 Overview of final rule

The key features of the more preferable final rule are:

- Retailers that are not wholly or partly government-owned or registered as a RoLR, or a related entity of those retailers, will be able to defer the payment of network charges to DNSPs incurred between 6 August 2020 and 6 February 2021 for eligible customers for six months. There is no provision in this rule to allow for an extension of this timeframe.
- Customers for which retailers will be able to defer the payment of network charges include residential and small business customers on a payment plan, hardship arrangement or deferred debt arrangement at the time the statement of charges relating to that customer is issued by the DNSP.
- Eligible retailers will be required to:
  - provide a statutory declaration to the DNSP verifying the customers for which a COVID-19 customer arrangement is in place and the amount of network charges payable in respect of those customers
  - pay interest on any deferred network charges at a rate of 3 per cent per annum.
- DNSPs will be able to defer the payment of a proportionate amount of transmission use of system (TUOS) charges to TNSPs, subject to a requirement that the DNSP pass through the corresponding amount of interest earned on deferred network charges to the TNSP. Further, the TNSP is not entitled to charge or recover any other or additional interest in respect of those charges (other than any interest charged under the connection agreement for late payment of TUOS charges).
- Participants are required to negotiate in good faith and agree on processes to give effect to the deferral mechanism under the final rule as soon as practicable, and in any case no later than 10 business days after the commencement date.
- Retailers will be required to report monthly to the AER on the number of customers whose network payments are deferred under the scheme, the total network payments deferred under the scheme and the latest due date for payment of those network charges. The AER will also be required to publicly report on this data each month.
- For the purposes of the credit support rules, the application of the deferral mechanism to any network charges must be taken into account in determining whether any amount is or remains outstanding, and in determining the time allowed for payment of network charges.

Further detail on the more preferable final rule can be found in the appendices.

### 3.4.2

#### **The Commission's rationale for the final rule**

Having regard to the issues raised in the rule change request and during consultation, the Commission is satisfied that the more preferable final rule is likely to better contribute to the achievement of the NEO.

The Commission considers that the implementation of a deferral mechanism with the design features discussed above is a necessary and proportionate response to the impacts of COVID-19 on the electricity market.

The final rule will achieve a number of key objectives, including:

- The deferral mechanism under the final rule will allow retailers to continue to support vulnerable customers while managing the inability to disconnect customers for non-payment in light of the AER's Statement of Expectations<sup>32</sup>. As discussed in section 3.3, the Statement of Expectations represents a change to the way risk is ordinarily allocated in the NEM in a manner which is outside of the control of retailers. In particular, the Statement of Expectations changes the risk profile of retailers by stipulating that they should not disconnect customers that may be financially vulnerable until 31 October 2020 and potentially beyond, where the relevant customer has contacted the retailer or is receiving any retailer support. The Commission considers that the deferral mechanism under the final rule is a targeted solution to help retailers manage this increased risk while continuing to supply electricity to vulnerable customers. Were the deferral mechanism not implemented, there would be a heightened risk of some retailers exiting the market due to a combination of the economic impacts of COVID-19 and the AER's expectations relating to customer disconnections during this period. The Commission therefore does not agree that retailers exiting the market in the short-term would be a natural outcome of competitive market forces.
- The final rule provides a framework to help manage potential increases in customer non-payment in the second half of 2020. The full economic impacts of COVID-19 on the electricity market, and the economy more broadly, remain unclear in severity and duration. However, available evidence suggests that these impacts will continue to manifest and potentially worsen over the next six months. The final rule helps mitigate this risk by providing for the deferral of network charges for eligible customers until February 2021. If further financial support for the retail market is needed beyond this period, including to help retailers manage increased bad debt risk, consideration of extending the deferral mechanism<sup>33</sup> or other policy measures to address this issue may be warranted.
- The customer eligibility requirements under the final rule also link the scope of the deferral mechanism to the scale of the impacts of COVID-19, as retailers are only able to defer network charges for the customers that are most likely to have been affected by the pandemic. Importantly, this ties the impacts of COVID-19, which are still uncertain, to the scale of the deferral mechanism and therefore provides a proportionate solution.
- The threat COVID-19 poses to the financial viability of some retailers could have implications for market competition and financial contagion in the NEM. The current level of competition in the retail market has taken many years to develop and it would not be in the long term interests of consumers for market competition to be reduced as a result of the short term impacts of COVID-19. This could result in a reduced range of offers, and potentially higher prices, being available to consumers. Should a number of smaller retailers exit the market, it would also likely take a number of years for the retail market to return to its current level of competition. The final rule helps mitigate this risk by

32 AER, *AER Statement of Expectations of energy businesses: Protecting consumers and the energy market during COVID-19*, 28 July 2020. Available at: <https://www.aer.gov.au/publications/corporate-documents/aer-statement-of-expectations-of-energy-businesses-protecting-consumers-and-the-energy-market-during-covid-19>.

33 A further rule change would be required to extend the deferral period under the final rule.



providing cash flow relief to those retailers that are more likely to be in financial distress, thereby providing those retailers with an opportunity to adjust their operations as required to respond to the pandemic and reducing the likelihood of those retailers exiting the market in the short term.

- The final rule imposes a number of limitations on the AER's proposal with respect to retailer eligibility, customer eligibility and deferral timeframes. This will allow the impacts of COVID-19 to be shared across parts of the electricity supply chain without imposing an unmanageable financial burden on network businesses. NSPs will be able to recover their efficient costs through the imposition of interest on any deferred network charges. This requirement also imposes incentives on retailers to manage their cash flow risk. The final rule also clarifies that NSPs will be able to recover the interest on any unpaid network charges if a retailer becomes insolvent. As such, the Commission does not consider that the effect of the deferral mechanism should be considered in future determinations of NSPs' WACC.

The Commission notes that the policy design choices under the final rule have been informed by the extraordinary circumstances associated with COVID-19 and the need to have a framework in place as quickly as possible to assist the market in dealing with the impacts of the pandemic. This rule change was assessed on an urgent basis in order to achieve this objective and the approach to determining eligibility criteria and implementation processes should therefore not be interpreted as setting a precedent for future decisions.

## 3.5 Implementation

The Commission considers it important that the deferral mechanism be implemented promptly to ensure a framework is in place to manage expected increases in customer debt. As such, the period in which retailers can defer network charges for eligible customers commences on 6 August 2020 and expires six months from this date (i.e. on 6 February 2020). The final rule requires participants to implement processes to give effect to the deferral mechanism within 10 business days of commencement.

Given the temporary status of the deferral mechanism, the final rule has been incorporated as transitional provisions in Chapter 11 of the NER that operate for the purposes of Chapter 6B. The Commission notes that Victoria has not adopted Chapter 6B of the NER, meaning the rule change does not apply in the Victorian region.

## ABBREVIATIONS

ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
Commission	See AEMC
DNSP	distribution network service provider
MCE	Ministerial Council on Energy
NEL	National Electricity Law
NEM	national electricity market
NEO	national electricity objective
NERL	National Energy Retail Law
NERR	National Energy Retail Rules
NSP	network service provider
RBA	Reserve Bank of Australia
RoLR	Retailer of Last Resort
TNSP	transmission network service provider
TUOS	transmission use of system
WACC	weighted average cost of capital

## A LEGAL REQUIREMENTS UNDER THE NEL

This appendix sets out the relevant legal requirements under the NEL for the AEMC to make this final rule determination.

### A.1 Final rule determination

In accordance with s. 102 of the NEL the Commission has made this final rule determination in relation to the rule proposed by the AER.

The Commission's reasons for making this final rule determination are set out in section 3.4.

A copy of the more preferable final rule is attached to and published with this final rule determination. Its key features are described in section 3.4.

### A.2 Power to make the rule

The Commission is satisfied that the more preferable final rule falls within the subject matter about which the Commission may make rules. The more preferable final rule falls within s. 34 of the NEL as it relates to:

- regulating the operation of the NEM<sup>34</sup>
- regulating the activities of registered participants participating or involved in the operation of the NEM<sup>35</sup>
- facilitating and supporting the provision of services to retail customers.<sup>36</sup>
- credit support arrangements between DNSPs and retailers.<sup>37</sup>

### A.3 Commission's considerations

In assessing the rule change request the Commission considered:

- its powers under the NEL to make the rule
- the rule change request
- submissions received during consultation
- the Commission's analysis as to the ways in which the proposed rule will or is likely to, contribute to the achievement of the NEO.

There is no relevant Ministerial Council on Energy (MCE) statement of policy principles for this rule change request.<sup>38</sup>

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34 s. 34(1)(a)(i) of the NEL.

35 s. 34(1)(a)(iii) of the NEL.

36 s. 34(1)(aa) of the NEL.

37 Item 26M of Schedule 1 of the NEL.

38 Under s. 33 of the NEL the AEMC must have regard to any relevant MCE statement of policy principles in making a rule. The MCE is referenced in the AEMC's governing legislation and is a legally enduring body comprising the Federal, State and Territory Ministers responsible for energy. On 1 July 2011, the MCE was amalgamated with the Ministerial Council on Mineral and Petroleum Resources. The amalgamated council is now called the Ministerial Forum of Energy Ministers (formerly COAG Energy Council).

## A.4 Civil penalties

The Commission cannot create new civil penalty provisions. However, it may recommend to the Ministerial Forum of Energy Ministers (formerly COAG Energy Council) that new or existing provisions of the NER be classified as civil penalty provisions.

The final rule does not amend any clauses that are currently classified as civil penalty provisions under the NEL or National Electricity (South Australia) Regulations. The Commission does not propose to recommend to the Ministerial Forum of Energy Ministers that any of the proposed amendments made by the final rule be classified as civil penalty provisions.

## A.5 Conduct provisions

The Commission cannot create new conduct provisions. However, it may recommend to the Ministerial Forum of Energy Ministers that new or existing provisions of the NER be classified as conduct provisions.

The final rule does not amend any rules that are currently classified as conduct provisions under the NEL or National Electricity (South Australia) Regulations. The Commission does not propose to recommend to the Ministerial Forum of Energy Ministers that any of the proposed amendments made by the final rule be classified as conduct provisions.

## B RETAILER ELIGIBILITY AND INCENTIVES

### B.1 Overview

The AER's rule change request proposed that all retailers be allowed to defer the payment of some network charges incurred between 1 July 2020 and 31 December 2020 for eligible customers for six months. However, the AER acknowledged that the application of the payment deferrals could be narrowed to certain retailers that satisfy reasonable conditions of accessing this support mechanism. The Commission considers that the materiality of the risk faced by retailers due to COVID-19 will differ between participants and some retailers should be better placed to absorb the cash flow impacts of the pandemic, or access alternative forms of cash flow support, than others.

This appendix sets out stakeholders' views on retailer eligibility requirements and the Commission's analysis and conclusions in respect of this issue.

### B.2 Proponent's views

The AER recommended in its submission to the consultation paper that retailers that are least likely to require financial support be restricted from accessing the deferral mechanism.<sup>39</sup> The AER supported achieving this by excluding government-owned retailers and retailers registered as a RoLR from being eligible to defer network charges under the final rule, noting that:<sup>40</sup>

- government-owned retailers have obvious channels of support through their shareholders, who can provide additional finance directly should these retailers experience financial distress
- registered RoLR retailers would also have access to credit through their parent companies, or at competitive rates from credit markets.

The AER considered that restricting these retailers from the mechanism would mitigate the impacts on networks and maximise the mechanism's value to customers by focusing explicitly on supporting retail sector competition.<sup>41</sup> The AER also recognised that it may be called upon to assess applications for support from otherwise restricted retailers if those retailers were allowed to apply for access to the deferral mechanism.<sup>42</sup>

The AER recommended imposing interest on deferred network charges and considered that the interest rate should be set at a material level, equivalent to that available to an entity with a sub investment grade credit rating.<sup>43</sup>

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39 AER, submission to consultation paper, p. 3.

40 Ibid.

41 Ibid.

42 Ibid.

43 Ibid.

## B.3 Stakeholder views

Most stakeholders commented in submissions to the consultation paper on whether access to the deferral mechanism should be narrowed to only retailers with a legitimate need for cash flow relief as a result of the impacts of COVID-19. Relevant comments are summarised below.

The majority of retailers, along with the Australian Energy Council, considered that the mechanism should be accessible to all retailers and did not support eligibility requirements that would differentiate between retailers based on size, ownership structure or other criteria.<sup>44</sup> Some retailers also expressed concerns that excluding certain retailers from accessing the mechanism would be inconsistent with the principles of a competitive market.<sup>45</sup> Retailers provided mixed views on whether it is appropriate to impose interest on deferred network charges. Some retailers considered this would provide appropriate incentives to retailers considering accessing the mechanism, while others considered this would impose undue costs on retailers.<sup>46</sup>

All network businesses, along with Energy Networks Australia, supported the adoption of retailer eligibility criteria in the final rule to limit access to the deferral mechanism to those retailers with a need for such support. A range of views were expressed about how this should be given effect, including:

- expressly excluding certain categories of retailer which could more easily access alternative sources of funds, including:
  - government-owned retailers
  - RoLR retailers
  - retailers listed on the Australian stock exchange or an overseas stock exchange
  - vertically integrated retailers
  - retailers with an investment-grade credit rating
- establishing eligibility criteria relating to a retailers' financial position and an independent verification process to determine whether a particular retailer meets those criteria.

Networks generally supported the imposition of interest on deferred network charges, with a number of stakeholders suggesting that a network's regulated WACC would appropriately reflect the business' financing costs.<sup>47</sup> It was also acknowledged that a fixed interest rate may be preferable to prevent additional complexity in the implementation of the mechanism. Some networks also suggested that, in order to access the mechanism, retailers should be required to establish that they will continue to be commercially viable after the expiry of the deferral mechanism to ensure there will be market competition benefits from providing cash flow support to a particular retailer.<sup>48</sup>

44 See for example, submissions to consultation paper: AEC, p. 4; AGL, p. 2; Amaysim, p. 3; ERM Power, p. 4; Next Business Energy, p. 4; Simply Energy, p. 3.

45 See for example, Red and Lumo, submission to consultation paper, p. 2.

46 See for example, submissions to consultation paper: AEC, p. 4; Alinta Energy, p. 2; Locality Planning Energy, p. 3.

47 See for example, submissions to consultation paper: Essential Energy, p. 9; ENA, p. 15.

48 See for example, ENA, submission to consultation paper, p. 13.

A number of consumer representatives commented on this issue and generally reflected similar views to those expressed by network businesses, suggesting that large retailers and/or retailers that could not establish a financial need should not be eligible to access the mechanism.<sup>49</sup>

The Queensland Government recommended that Tier 1 and government-owned retailers (either partly or wholly) be excluded from the rule change on the basis that these businesses should have sufficient financial backing to address customer non-payment issues within a reasonable period.<sup>50</sup>

A number of stakeholders also commented on the proposed policy position set out in the directions paper published on 9 June 2020, which indicated that retailers registered as RoLRs and government-owned retailers would be ineligible to access the deferral mechanism under the final rule. Some large retailers opposed this proposal in submissions to the directions paper on the basis that it would risk distorting competitive market forces.<sup>51</sup> Network businesses and consumer groups generally supported the proposed approach and agreed with the rationale set out in the directions paper.<sup>52</sup>

Some stakeholders also commented in submissions to the directions paper on the proposal to impose interest on deferred network charges at a rate of 3% per annum. It was suggested by some NSPs that this rate may be too low to impose appropriate incentives on retailers and that the NSP's WACC determined by the AER would be a more appropriate rate.<sup>53</sup>

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49 See for example, EUAA, submission to consultation paper, p. 2.

50 QLD Government, submission to consultation paper, p. 2.

51 See for example, submissions to directions paper: Origin Energy, p. 1; AGL, p. 1.

52 See for example, submissions to directions paper: ECA, p. 1; Ausgrid, p. 1; SAPN, p. 1.

53 See for example, submissions to directions paper: SAPN, p. 2; Endeavour Energy, p. 2.

## B.4 Commission's analysis and conclusions

### BOX 2: FINAL RULE

The final rule provides that government-owned retailers (whether wholly or partly owned) and retailers registered as a Retailer of Last Resort (RoLR) in any jurisdiction, including their related entities, will not be eligible to defer the payment of network charges, given that these retailers should be in a strong position to access other forms of cash flow relief if required. All retailers not falling into these two categories will be eligible to utilise the deferral mechanism.

Eligible retailers will be required to pay interest on any deferred network charges at a rate of 3.00% per annum.

#### **Benefits of final rule**

The Commission considers that the combination of the retailer eligibility criteria and the obligation to pay interest on deferred charges will result in the cash flow relief provided by the deferral mechanism being accessed by retailers that are in legitimate financial need and/or cannot feasibly access alternative sources of funds.

The Commission considers it appropriate to limit access to the financial support provided by the deferral mechanism to those retailers that have the greatest need for this support as a direct result of the COVID-19 pandemic. It is also important to consider the nexus between the retailer eligibility criteria and the financial impact of the deferral mechanism on network businesses. The final rule achieves this by providing that retailers that are government-owned (either wholly or partly) and retailers registered in any region as a Retailer of Last Resort (RoLR) (as well as any related entities of these retailers) will be excluded from deferring the payment of network charges. The Commission considers that retailers falling into these two categories should be in a strong financial position and/or able to access alternative sources of credit to alleviate any cash flow issues they are currently experiencing. The final rule also requires that eligible retailers pay interest on any deferred network charges at a rate of 3.00% per annum. The above requirements are consistent with the positions proposed in the directions paper published on 9 July 2020. While the Commission acknowledges that some stakeholders disagreed with these requirements in submissions, the rationale for maintaining these requirements under the final rule is discussed further below.

#### **Exclusion of RoLR retailers**

The AER's Retailer of Last Resort statement of approach states that the RoLR scheme should result in the appointment of designated RoLRs with the financial and organisational capacity to carry out the role.<sup>54</sup> In appointing default RoLRs, the AER considers a retailer's ability to access potentially large financial resources at short notice. The rationale and criteria for appointing a retailer as a RoLR therefore indicates that RoLR retailers should not need to

<sup>54</sup> AER, *Retailer of Last Resort statement of approach*, November 2011. Available at: <https://www.aer.gov.au/retail-markets/retail-guidelines-reviews/retailer-of-last-resort-guideline-plan-and-statement-of-approach>.



access the proposed deferral mechanism. In particular, the Commission considers that, given their size, financial capacity and access to capital, currently registered RoLR retailers should be able to absorb any cash flow impacts of COVID-19 without resorting to deferring the payment of network charges. The objective of this rule change is to support retailers to continue to supply vulnerable customers in the immediate term while managing the changes to their risk profile in circumstances where alternative forms of cash flow relief are unlikely to be accessible. The Commission considers that allowing RoLR retailers to access payment deferrals would be inconsistent with the above objective and would not be in the long term interests of consumers. On that basis, the Commission considers determining eligibility by reference to the RoLR framework to be an appropriate and pragmatic approach.

### **Exclusion of government-owned retailers**

The Commission considers that similar logic applies to government-owned retailers. To the extent that these retailers are experiencing cash flow challenges, this should be addressed through financial support provided by the relevant government in the first instance. This is consistent with the principle that retailers that are able to access viable alternative sources of additional funds should not require support through the mechanism. The Commission notes that this is consistent with the position expressed by the Queensland Government and the AER in their submissions to the consultation paper.

### **Interest rate**

Retailers that do not fall into the two excluded categories identified above will automatically be eligible to defer the payment of network charges for eligible customers (discussed further below). Given that a range of retailers comprising different customer bases, ownership structures and asset portfolios will be eligible, the Commission considers it necessary to incentivise only those retailers that have a legitimate need for cash flow relief, and limited options for obtaining such relief, to access the deferral mechanism.

To facilitate this, eligible retailers will be required to pay interest on any deferred network charges at a rate of 3% per annum.

The Commission engaged HoustonKemp to undertake analysis and provide advice on the appropriate interest rate to impose on deferred network charges, having regard to the objectives of this element of the deferral mechanism. HoustonKemp's report is available on the project page on the AEMC's website. The determination of the interest rate has been informed by the following considerations:

- The Commission has considered business lending rates for recently funded new loans in order to determine the level of interest payable that is likely to impose appropriate incentives on retailers considering utilising the deferral mechanism. In particular, the interest rate should be set at a level that would encourage retailers that are able to secure additional credit from the market to pursue this option before resorting to deferring the payment of network charges.
- Analysis of business lending rates supports an interest rate on deferred network charges of 3% per annum, given that this interest rate is likely to be:
  - lower than the lending rate currently available to a small retailer in the NEM

- higher than the lending rate currently available to some larger retailers in the NEM that are in a stable financial position but still meet the retailer eligibility criteria discussed above – these retailers are likely to be able to borrow funds more cheaply than a small retailer.
- The estimates of variable business lending rates for small, medium and large businesses that have informed this analysis are set out in Table B.1 below.

**Table B.1: Variable business lending rates for new loans funded in the month (per annum)**

DATE	SMALL	MEDIUM	LARGE
31/01/2020	3.81%	2.53%	2.22%
29/02/2020	3.93%	2.66%	2.24%
31/03/2020	3.63%	2.40%	1.91%
30/04/2020	4.37%	2.28%	1.67%

Source: HoustonKemp, based on business loan rates reported by the RBA in 2020.

Note: Small businesses are defined as those receiving funding less than \$1m and with turnover less than \$50m. Medium businesses are defined as those receiving funds greater than \$1m and with turnover less than \$50m. Large businesses are defined as those with turnover greater than \$50m.

- The rates presented in Table B.1 indicate that an interest rate of 3% per annum is likely to sit in between the rates currently available to small businesses (i.e. the smaller retailers that are likely to access the deferral mechanism) and medium/large businesses, which would likely be able to access credit from the market at a lower rate. This is consistent with the objectives of the interest rate described above.
- Some stakeholders suggested the applicable regulated weighted average cost of capital (WACC) for each DNSP could be an appropriate interest rate to apply to deferred payments.
- However, the rate of return earned by a DNSP is not the WACC determined by the AER but is instead the out-turn inflation adjusted WACC. This is because the regulatory regime protects distributors from unforeseen inflation outcomes by:
  - providing a real return on capital in the annual revenue requirement of the distributor, through the removal of the expected inflation indexation of the regulated asset base (RAB) from the return on capital building block
  - indexing the RAB for out-turn inflation in the roll forward
  - indexing prices during the regulatory period for lagged out-turn inflation.
- It would therefore be necessary to use the inflation adjusted WACC to accurately reflect the rate of return earned by a DNSP. However, the inflation figures required to calculate the actual inflation adjusted WACC applying during the deferral period for each DNSP will not be published by the Australian Bureau of Statistics until late January 2021. As such, an interest rate based on the actual inflation adjusted WACC for each DNSP could not be calculated with certainty at the commencement of the deferral mechanism.

- While the actual inflation adjusted WACC of each DNSP could not be calculated until January 2021, an estimate of this figure can be calculated based on inflation forecasts published by the Reserve Bank of Australia. This approach can be used to calculate the *estimated* inflation adjusted WACC for each DNSP. When using this methodology, the median estimated inflation adjusted WACC across all DNSPs that will be subject to the final rule is 3.00% per annum. This rate is therefore approximately reflective of what the inflation adjusted WACC of a DNSP that is subject to the rule is likely to be.

Based on the above analysis, the Commission considers that an interest rate of 3% will achieve a number of key objectives:

- Eligible retailers that can secure credit at an interest rate below 3% will have a financial incentive to try to obtain additional funds from the private sector prior to accessing the deferral mechanism.
- Networks will be able to recover the direct costs they are likely to incur as a result of the deferral of these payments.
- Eligible retailers will face an efficient price signal because they will be paying the cost of the finance that the DNSP is likely to incur.
- A fixed rate avoids the need for adjustments which would result from any difference in the rate the retailer is required to pay and the rate the DNSP is entitled to recover. This approach is also administratively simple and therefore aligns with the objective of allowing the deferral mechanism to be implemented and utilised as soon as possible.

The intent of the proposed rule is that any interest payments received by an NSP would not be counted as revenue for the purpose of the NSPs' maximum allowed revenue (MAR). The Commission also expects retailers not to seek to pass through any interest costs to customers. In addition, in the event that a retailer that has deferred the payment of some network charges subsequently goes insolvent before paying those charges, the DNSP would be entitled to recover the interest on those deferred network charges through the existing process applying for a retailer insolvency pass-through event.

### **Consideration of alternative approaches**

The Commission considered a number of alternative approaches for setting eligibility criteria for retailers. The options considered and the rationale for rejecting these options are summarised below:

- Independent assessment of financial need - Retailers could be required to provide information for an independent assessment of whether they meet specified financial criteria. These criteria would need to be established beforehand and would likely relate to debt levels and cash flow metrics. This approach was not adopted for this rule change because it would require a more onerous administrative process to be developed and implemented, which would impede participants' ability to facilitate payment deferrals in a timely manner. The Commission therefore does not consider that this approach would be consistent with the objective of providing cash flow relief to eligible retailers as soon as possible.

- Stock market listing - Publicly listed retailers could be excluded from the deferral mechanism. This criteria would capture a range of retailers with a wide variation in size and asset portfolios and would not capture large retailers operating in the NEM that are not publicly listed. The Commission therefore does not consider this would be a suitable basis on which to determine eligibility.
- Credit rating - Retailers with an investment grade credit rating, or a rating above a certain threshold, could be excluded from the mechanism. Credit ratings are only available for a small number of retailers in the NEM and these ratings are assessed differently by different ratings agencies. The Commission considers the approach taken under the final rule to be a simpler and more transparent option for determining retailer eligibility.
- Customer base - Retailers with a customer base above a certain threshold could be excluded from the mechanism. However, this would require the arbitrary determination of a specific customer base above which a retailer is not entitled to cash flow relief under the final rule. The Commission does not consider this to be a sufficiently robust approach to determining retailer eligibility.

The Commission considers that the combination of the explicit eligibility criteria specified in the final rule and the requirement to pay interest on deferred network charges imposes appropriate entry requirements and incentives on retailers while still allowing payment deferrals to be administered in a timely manner.

## C CUSTOMER ELIGIBILITY

### C.1 Overview

Social and policy measures implemented in response to the COVID-19 pandemic are likely to have impacted on some customers' ability to pay their electricity bill. These non-payment issues are likely to continue to manifest over the next six months as the economic impacts of the pandemic become more apparent. The determination of which of their customers retailers should be able to defer the payment of network charges for is therefore an important consideration in the design of the deferral mechanism. This is necessary to ensure that the relief provided by this rule change is effective and appropriately targeted.

This appendix sets out stakeholders' views on the customer eligibility criteria and the Commission's analysis and conclusions on this issue.

### C.2 Proponent's views

The AER did not comment on the customer eligibility requirements in its submission to the consultation paper.

### C.3 Stakeholder views

Most stakeholders commented on the customer eligibility requirements in submissions to the consultation paper. Relevant comments are summarised below.

Retailers generally agreed with the AER's proposal to extend eligibility to all customers on a payment plan, hardship arrangement or deferred debt arrangement. However, most retailers suggested that the eligibility criteria should not exclude customers that were on these arrangements prior to the pandemic (i.e. before 1 March 2020), as these customers were already vulnerable before COVID-19 and are arguably in need of the most assistance now.<sup>55</sup> Some retailers also opposed excluding large customers from the deferral mechanism, suggesting that the operations of many commercial and industrial customers have been significantly impacted by COVID-19 and retailers do not always hold adequate security to account for bad debt from these customers.<sup>56</sup>

Network business generally considered that the deferral mechanism should only apply to residential and small business customers, as these are the customers to which the restriction on disconnections under the AER's Statement of Expectations applies.<sup>57</sup> Some networks also suggested that there should be some requirement to demonstrate that eligible customers have entered onto these payment arrangements as a result of COVID-19.<sup>58</sup>

Consumer representatives considered that eligibility for payment deferrals should extend to customers that were on the relevant payment arrangements prior to COVID-19. The Energy

<sup>55</sup> See for example, submissions to consultation paper: AEC, p. 4; Alinta Energy, p. 2; EnergyAustralia, p. 9; Origin Energy, p. 3.

<sup>56</sup> See for example, ERM Power, submission to consultation paper, p. 5.

<sup>57</sup> See for example, submissions to consultation paper: ENA, p. 14; Ausgrid, p. 10; Endeavour Energy, p. 1.

<sup>58</sup> See for example, SAPN, submission to consultation paper, p. 13.

Users Association of Australia also submitted that large customers should be included in the deferral mechanism, subject to satisfying certain conditions.<sup>59</sup>

## C.4 Commission's analysis and conclusions

### BOX 3: FINAL RULE

The final rule allows eligible retailers to defer the payment of network charges incurred in respect of residential and small business customers that are on a payment plan, hardship arrangement or deferred debt arrangement at the time the statement of charges applying to that customer is issued by a DNSP.

#### Benefits of final rule

The final rule will make sure that retailers are able to defer the payment of network charges for customers that are most likely to be experiencing payment difficulties as a result of COVID-19. The rule achieves this in a way which is transparent and should allow participants to leverage existing processes developed to implement the Network Relief Package.

The Commission considers that the deferral mechanism should capture customers:

- whose ability to pay their electricity bill is most likely to have been impacted by COVID-19
- for whom retailers do not hold security or have the option of disconnecting for non-payment.

The AER's rule change request proposed that eligible customers be defined as those that enter into a payment plan, hardship arrangement or deferred debt arrangement between 1 March 2020 and 31 December 2020. The Commission agrees that customers on payment plans and hardship arrangements are likely to be the most financially vulnerable class of customers and therefore the most likely to be facing challenges paying their electricity bill as a result of COVID-19. However, the Commission also understands that many retailers have implemented COVID-19-specific deferred payment arrangements to assist customers during this period. This is likely to have contributed to the lower than expected increases in the number of customers on payment plans and hardship arrangements being reported by retailers to the AER in recent months.<sup>60</sup> It is important that the deferral mechanism captures this third category of customers in order to allow retailers to effectively support the range of customers that are most impacted by COVID-19. The final rule therefore allows retailers to defer the payment of network charges for customers on a "COVID-19 customer arrangement", which are customers that are on a payment plan, hardship arrangement or deferred debt arrangement at the time the statement of charges applying to that customer is issued to the retailer. In addition, the definition of "deferred debt arrangement" in the final

<sup>59</sup> EUAA, submission to consultation paper, p. 3.

<sup>60</sup> The AER has called on retailers to provide additional data on a voluntary basis to enable us to have visibility of the effect of COVID-19 on the retail energy market. The data provides a high-level summary of changes in the retail market and is updated weekly. See <https://www.aer.gov.au/retail-markets/performance-reporting/weekly-retail-market-dashboards-covid-19>.

rule makes clear that customers on such arrangements must be experiencing payment difficulties in order to fall within this definition. The customer eligibility requirements therefore link the scope of the deferral mechanism to the scale of the impacts of COVID-19, as retailers are only able to defer network charges for the customers that are most likely to have been affected by the pandemic.

The Commission does not consider that it is appropriate to limit the support provided by the deferral mechanism to customers that entered into such arrangements from March 2020 onward. Such a definition would exclude customers that were already on these types of payment arrangements prior to COVID-19 and were thus already financially vulnerable. These customers may be at an even higher risk of being unable to pay their bills due to the economic impacts of the pandemic on their already vulnerable circumstances. In addition, the prohibition on disconnections in the AER's Statement of Expectations is not limited to customers that entered into certain payment arrangements from March 2020 onward. The final rule therefore also allows retailers to defer the payment of network charges in respect of these customers. While this will result in a slightly higher proportion of customers being eligible for deferrals than the AER's proposed definition, this will still be a very small proportion of overall customers (approximately 2 per cent of residential customers) and the resulting cash flow deferrals are considered to be manageable for NSPs.

The definition of "COVID-19 customer arrangement" in the final rule only includes small customers, as defined in the National Energy Retail Law (NERL). In effect, this captures residential and business customers with an annual electricity consumption below the statutory thresholds determined in each jurisdiction that has adopted the NERL. The Commission considers that retailers can manage cash flow issues relating to large customers through their commercial arrangements with those customers, including by drawing on security provided by those customers. In addition, the prohibition on disconnection in the AER's Statement of Expectations does not apply to large customers. As such, the Commission does not consider it appropriate or necessary for the deferral mechanism to apply to large customers. The existing consumption thresholds for small customers under the NERL (as applied in relevant participating jurisdictions) are considered to be an appropriate and transparent reference point for differentiating between small and large customers in this context.

## D DEFERRAL TIMEFRAME AND TERMS

### D.1 Overview

The purpose of this rule change is to assist retailers to continue to support vulnerable customers while dealing with the immediate cash flow impacts of COVID-19 and the requirements under the AER's Statement of Expectations. It is impossible to predict with certainty how the impacts of the pandemic will continue to manifest over the next 12 months and the specific implications this will have for the energy sector. The appropriate timeframe for the deferral of network charges must therefore be based on a reasonable assessment of the likely period during which the cash flow relief provided by the deferral mechanism will continue to be an appropriate method for supporting the retail market, having regard to the overarching objective of the rule change.

This appendix discusses stakeholder's views on the deferral timeframe and the Commission's analysis and conclusions on this issue.

### D.2 Proponent's views

In its submission to the consultation paper, the AER maintained that the decision on whether to extend the deferral period beyond 31 December 2020 should be at the AER's discretion in order to retain the flexibility to respond to the circumstances of the NEM and broader Australian economy at that time.<sup>61</sup> The AER noted that in forming a view as to whether it is necessary to extend this period it would monitor retail market dynamics and take-up of the deferral mechanism during its initial six month phase.<sup>62</sup> The AER also suggested it would undertake some form of stakeholder consultation in making this decision, but that this process may be abbreviated given the timeframes involved.<sup>63</sup>

### D.3 Stakeholder comments

Comments in submissions to the consultation paper on the deferral timeframe and terms are summarised below.

Most retailers suggested that six months is appropriate as a minimum deferral period and that a longer timeframe may be necessary to address the impacts of COVID-19.<sup>64</sup> Retailers again cited the risks posed by existing financial support measures being withdrawn in the second half of 2020 in this context. Most, though not all, retailers also supported the AER having the power to extend the deferral period beyond the initial six month timeframe. It was also suggested that the duration of the AER's Statement of Expectations is a relevant consideration in determining the length of the deferral period.<sup>65</sup>

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<sup>61</sup> AER, submission to consultation paper, p. 4.

<sup>62</sup> Ibid.

<sup>63</sup> Ibid.

<sup>64</sup> See for example, submissions to consultation paper: AEC, p. 5; Amaysim, p. 3; ERM Power, p. 5; Origin Energy, p. 3.

<sup>65</sup> Simply Energy, submission to consultation paper, p. 6.



Some network businesses suggested that six months is an appropriate deferral period based on currently available information, while others considered that a shorter deferral period would be more reasonable.<sup>66</sup> Networks were generally opposed to the AER having the power to extend the deferral period beyond 31 December 2020. It was suggested that this would create additional uncertainty for NSPs and may impact on their credit rating, given that a longer deferral period would result in more significant cash flow impacts for network businesses. Some networks suggested that, if the AER were to be given the ability to extend the timeframe, this should be subject to stringent consultation requirements to ensure the process is considered and transparent.<sup>67</sup> Alternatively, others suggested that any extension of this timeframe should be subject to a further rule change by the AEMC.<sup>68</sup>

Consumer representatives generally supported the AER's proposal of an initial six month deferral period, with the AER having the option to extend this timeframe if necessary.<sup>69</sup>

The Queensland Government supported a maximum deferral period of six months, on the basis that this would provide support to businesses that will likely still be in recovery in the second half of 2020.<sup>70</sup> The Queensland Government did not support the AER having the ability to extend the deferral period, noting that if a further six months is required, then a broader government response may be needed.<sup>71</sup>

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66 See for example, submissions to consultation paper: Endeavour Energy, p. 1; Essential Energy, p. 5; SAPN, p. 14; Spark Infrastructure, p. 3.

67 See for example, submissions to consultation paper: Spark Infrastructure, p. 3; Ausgrid, p. 12.

68 Essential Energy, submission to consultation paper, p. 6.

69 See for example, submissions to consultation paper: ECA, p. 3; EUAA, p. 1.

70 Queensland Government, submission to consultation paper, p. 2.

71 Ibid.

## D.4 Commission's analysis and conclusions

### BOX 4: FINAL RULE

Eligible retailers will be able to defer the payment of network charges incurred for eligible customers for a period of six months commencing on 6 August 2020. The due date for payment of these network charges will be deferred for a period of six months. The AER will not have the discretion to extend the deferral period. Participants are required to implement processes to give effect to the deferral mechanism within 10 business days of commencement of the final rule.

#### **Benefits of final rule**

A deferral period of six months from the commencement of the final rule is an appropriate timeframe to allow retailers to adjust their operations as needed to manage the immediate impacts of COVID-19 and the requirements of the current version of the AER's Statement of Expectations. Prescribing a fixed period for the payment deferrals (i.e. which is not subject to extension) also provides certainty to participants about the scope and purpose of the deferral mechanism.

### D.4.1 Deferral timeframes

There are two elements relating to the deferral timeframe which must be considered:

1. the period during which network charges can be deferred
2. the length of time the payment of those network charges can be deferred for.

With respect to the first point, the Commission considers that a period of six months from the commencement of the final rule is an appropriate timeframe to allow for network charges to be deferred. The deferral period will therefore commence on 6 August 2020 and expire on 6 February 2021. This will assist eligible retailers to manage the immediate cash flow impacts of COVID-19 and continue to focus on the supply of electricity to vulnerable customers during this period. This deferral period will also address concerns raised by many stakeholders that the economic impacts of COVID-19 will continue to manifest in many sectors of the economy during the second half of 2020. In particular, the Commission notes that:

- A number of existing financial support measures are scheduled to expire or be wound back during this period, including reductions to payments under the Federal Government's JobKeeper and JobSeeker payment scheme and the expiry of mortgage deferrals implemented by Australian banks in September 2020. It is reasonable to expect that some electricity customers will experience increased difficulty paying their bills once the financial support currently being provided by these schemes is removed.
- The AER's Statement of Expectations has been extended beyond 31 July 2020. The current version of the Statement of Expectations, published on 28 July 2020, still includes a modified prohibition on disconnection of customers for non-payment. Specifically, the Statement of Expectations stipulates that retailers are expected not to disconnect any

residential or small business customer that may be in financial distress and who has made contact with the retailer or is receiving any retailer support before 31 October 2020. The updated Statement of Expectations is somewhat less onerous for retailers in the sense that it allows them to disconnect non-paying customers where those customers have not contacted the retailer. This was identified as a key concern by a number of retailers in submissions to the consultation paper. However, retailers still need to manage a change in their risk profile as they are still expected to continue supplying many financially vulnerable customers having payment difficulties until the end of October 2020 (and potentially beyond).

- The intention of the AER's rule change proposal was to allow the deferral mechanism under the final rule to take effect from the date the Network Relief Package ceased to have effect, such that there was no gap in the provision of cash flow support to retailers. However, the end date of the period during which retailers can claim relief under the Network Relief Package differs depending on the region. In practice the Network Relief Package did not cease to have effect on 30 June 2020, as in some cases a retailer could claim relief in relation to a statement of charges issued up until mid-August 2020. The Commission therefore does not consider that the deferral period commencing in on 6 August 2020 will pose a material risk to retailers, particularly given the evidence suggests that the most severe impacts of COVID-19 may be yet to materialise.

Providing for the deferral mechanism to have effect for six months from 6 August 2020 therefore gives retailers the flexibility needed to continue to support vulnerable customers while managing the impacts of the pandemic and the AER's Statement of Expectations. The Commission notes that the purpose of this rule change is not to address bad debt risk or the medium to long-term implications for the energy sector of a broader economic recession. To the extent that broader economic outcomes continue to pose a material risk to the viability of the retail market in early 2021, it may be appropriate to consider an extension of this mechanism<sup>72</sup> or alternative policy measures to address this issue may be warranted.

In addition to the rationale set out above, the Commission considers that the deferral of some cash flows under the mechanism for six months should be manageable for network businesses (particularly given the eligibility criteria for retailers) based on analysis and feedback provided by stakeholders.

With respect to the length of time the payment of network charges can be deferred for, the Commission considers that deferring the due date for payment by six months will provide sufficient time for retailers to adjust their operations as needed to manage the immediate impacts of COVID-19. The final rule therefore provides that the due date for the payment of deferred network charges is taken to be six months from the date of issue of the relevant statement of charges. The Commission notes that retailers are not prevented from paying any deferred network charges before the deferred due date, should they choose to do so.

Figure D.1 provides a visual illustration of the deferral timeframes under the final rule.

<sup>72</sup> A subsequent rule change would be required to extend the deferral mechanism

**Figure D.1: Deferral timeframes under final rule**



## D.4.2

### Extension by the AER

The AER proposed in its rule change request that it have the discretion to extend the period during which retailers can defer the payment of network charges beyond six months if it considers it reasonable to do so. The final rule does not confer this discretion on the AER. Leaving open the possibility of requiring network businesses to defer the payment of network charges beyond February 2021 would introduce significant uncertainty for those participants. It is also not clear based on the evidence currently available that this will continue to be an appropriate or necessary measure to deal with the longer-term impacts of COVID-19. In addition, the deferral period under the final rule extends beyond the period proposed by the AER. Specifically, the rule change request proposed that the initial deferral period expire on 31 December 2020, whereas the deferral period under the final rule expires on 6 February 2021. As such, the final rule will provide additional time for retailers to adjust their operations to manage the impacts of COVID-19 prior to the expiry of the deferral mechanism. The Commission considers that this reduces the need to provide for any future extension of the deferral period.

The Commission notes that:

- it generally does not consider that payment deferrals should be an ongoing feature of the retail market, as it is up to retailers to determine how to manage cash flow issues in the medium to long term, including in response to broader economic recessions.
- if it becomes apparent in late 2020 that it may be necessary to extend the deferral period beyond six months, this could be considered at that point in time through an expedited rule change process, should the relevant statutory test be satisfied.

## E DEFERRAL OF PAYMENTS BETWEEN DNSPS AND TNSPS

### E.1 Overview

It is appropriate to consider whether, as part of the mechanism under the final rule, DNSPs should be entitled to defer the payment of TUOS charges to TNSPs for eligible customers and if so, how this should be addressed in the regulatory framework.

This appendix sets out stakeholders' views on the deferral of payments between DNSPs and TNSPs and the Commission's analysis and conclusions on this issue.

### E.2 Proponent's views

The AER did not comment on this issue in its submission to the consultation paper.

### E.3 Stakeholder views

Stakeholder feedback in submissions to the consultation paper on this issue was primarily provided by network businesses. The vast majority of stakeholders supported DNSPs being able to defer the payment of TUOS charges to TNSPs.<sup>73</sup> These stakeholders considered it appropriate for the cash flow impacts of the deferral mechanism to be shared between DNSPs and TNSPs and suggested that high level obligations giving effect to this should be imposed on these participants under the NER. Network businesses did not consider that the rules should be prescriptive about the processes used to implement this arrangement between DNSPs and TNSPs. Instead, they suggested that the rules should allow for flexibility in the way this arrangement is implemented, with some stakeholders noting that existing processes used to implement the Network Relief Package could be adapted for this purpose.

### E.4 Commission's analysis and conclusions

#### BOX 5: FINAL RULE

The final rule allows DNSPs to defer the payment of TUOS charges to TNSPs in proportion to the total network charges deferred by a retailer.

#### **Benefits of final rule**

This approach will materially reduce the impact of the rule change on DNSPs' cash flows by allowing the deferrals to be shared across the network supply chain.

The Commission considers it appropriate that the impact of payment deferrals be shared between DNSPs and TNSPs. The Commission notes that TUOS charges account for

<sup>73</sup> See for example, submissions to consultation paper: Ausgrid, p. 13; ENA, p. 15; TransGrid, p. 4.

approximately 14% of the total network charges applying to an average residential customer's electricity consumption.<sup>74</sup> Allowing DNSPs to defer the payment of TUOS charges in proportion to the network charges deferred by a retailer will therefore substantially reduce the cash flow impact of this rule change on DNSPs. The Commission considers that it is practical and appropriate for TNSPs and DNSPs to agree on processes to facilitate these deferrals, rather than seeking to prescribe these arrangements in the NER.

To give effect to the policy intent, the final rule:

- imposes a general requirement that provides for the payment of TUOS charges to be deferred by a DNSP in the circumstances described above
- requires TNSPs and DNSPs to negotiate in good faith to implement arrangements that facilitate this as soon as practicable after the commencement of the final rule
- requires DNSPs to pass through interest earned on the TUOS portion of any deferred network charges to TNSPs.

The Commission notes that DNSPs and TNSPs broadly expressed support for this approach in submissions to the consultation paper.

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<sup>74</sup> Based on analysis included in the Commission's 2019 Residential electricity price trends review.

## F PRACTICAL IMPLEMENTATION OF PAYMENT DEFERRALS

### F.1 Overview

The Commission considers it important that deferrals of network charges be implemented as quickly and effectively as possible once the final rule commences in order to ensure that retailers have access to timely cash flow relief to manage the impacts of COVID-19. A flexible approach is needed to accommodate the requirements of different participants and reduce any implementation costs associated with the deferral mechanism.

This appendix sets out stakeholders' views on the appropriate implementation process and the Commission's analysis and conclusions on this issue.

### F.2 Proponent's views

The AER did not comment on this issue in its submission to the consultation paper.

### F.3 Stakeholder views

A number of stakeholders commented on how the rules should address the processes for implementing the deferral mechanism. Relevant comments are summarised below.

The vast majority of stakeholders that commented on this issue suggested that the rules should not prescribe detailed requirements about how the deferral of network charges are to be administered by participants.<sup>75</sup> These stakeholders generally considered that it would be more pragmatic and feasible for network businesses and retailers to negotiate and agree on the relevant processes. Most participants suggested that the existing processes which have been agreed upon to implement the relief measures under the Network Relief Package could be leveraged or adapted to implement the deferral mechanism. However, some stakeholders noted challenges created by the inconsistency of these processes across regions and suggested that a more uniform approach would be preferable.<sup>76</sup>

Some network businesses also suggested that retailers should be required to submit a statutory declaration verifying the eligibility of customers for which they are claiming deferrals.<sup>77</sup>

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<sup>75</sup> See for example, submissions to consultation paper: AGL, p. 2; Endeavour Energy, p. 16; EnergyAustralia, p. 13; Simply Energy, p. 8.

<sup>76</sup> See for example, submissions to consultation paper: AGL, p. 2; Simply Energy, p. 8.

<sup>77</sup> See for example, ENA, submission to consultation paper, p. 16.

## F.4 Commission's analysis and conclusions

### BOX 6: FINAL RULE

Eligible retailers and DNSPs are required to cooperate in good faith to agree on and implement processes to give effect to the deferral mechanism under the final rule as soon as practicable, and no later than 10 business days after the commencement date of the final rule. Eligible retailers must provide a statutory declaration verifying that a COVID-19 customer arrangement is in place for each customer for which it is claiming a deferral and the amount of network charges payable for those customers.

#### **Benefits of final rule**

The final rule provides a pragmatic and flexible approach which allows participants to agree on processes for implementing the deferral mechanism, rather than seeking to prescribe these processes in the NER. This mitigates the risk of participants being unable to comply with detailed procedural requirements in the rules while also allowing the deferral mechanism to be implemented and utilised efficiently.

For the deferral mechanism to be effective, it is important that the processes used to administer payment deferrals are transparent, pragmatic and efficient. The Commission does not consider that it would be practical or appropriate for these processes to be prescribed in detail in the NER. This is consistent with feedback provided by stakeholders in submissions to the consultation paper.

The Commission understands that:

- some retailers and NSPs have already undertaken a process of negotiating and agreeing on processes to implement the support measures provided under the Network Relief Package - although the Commission notes that not all retailers sought to access relief under this package and the package did not apply in some regions in which the final rule will apply
- these existing processes can be leveraged to allow for payment deferrals under the final rule to be implemented and administered efficiently.

The final rule therefore does not include prescriptive requirements about the processes participants must use to give effect to the rule. Rather, retailers and NSPs are required to agree on such processes within 10 business days of the commencement of the rule. This timeframe balances feedback from network businesses in submissions to the directions paper regarding the timeframes in which it would be feasible for retailers and DNSPs to agree on and implement the required processes in each region with the need for these processes to be in place as soon as practicable.<sup>78</sup>

The final rule also requires eligible retailers to provide a statutory declaration confirming those customers that satisfy the eligibility requirements and the amount of network charges

<sup>78</sup> Submissions to directions paper: ENA, p. 5; SAPN, p. 3.



payable in respect of those customers within 10 business days of a statement of charges being issued. The Commission considers that this is appropriate to facilitate the payment deferrals being processed expediently while still providing DNSPs with some assurance that the relevant customers are eligible for deferrals under the rules. This is also similar to the assurance retailers are required to provide to DNSPs to access support under the Network Relief Package. The timeframe within which retailers must provide the statutory declaration has also informed the timeframe within which participants must implement processes to give effect to the deferral mechanism (as discussed above). This means that if a DNSP were to issue a statement of charges at the commencement of the deferral period (i.e. on 6 August 2020), the relevant processes would need to be in place by the date on which the retailer would also need to submit the relevant statutory declaration to the DNSP (thereby ensuring alignment between these two timeframes).

## G REPORTING REQUIREMENTS

### G.1 Overview

In order to provide transparency regarding the uptake and impact of the deferral mechanism under the final rule, it is important to consider the types of information participants may be required to provide in this regard and how such information can be made available to the market.

This appendix sets out stakeholders' views on potential reporting requirements under the final rule and the Commission's analysis and conclusions on this issue.

### G.2 Proponent's views

The AER recommended in its submission to the consultation paper that all affected participants under the scheme be required to report regularly to the AER on information relating to the uptake of the deferral mechanism, which may include the number of customers whose network payments have been deferred and the total network payments deferred under the scheme.<sup>79</sup> The AER suggested this would improve the transparency of the deferral mechanism for participants and that the information could also be used to inform any decision on the potential extension of the deferral period.

### G.3 Stakeholder views

Most stakeholders did not comment on reporting requirements associated with the deferral mechanism in submissions to the consultation paper. The ENA suggested that the AER should be required to prepare a report at the end of the deferral period identifying:<sup>80</sup>

- an estimate of the total net financial cashflow benefit provided to energy retailers under the rule arrangements
- any material discrepancies in the operation of the scheme
- any retail firm that has implemented disconnection and hardship approaches that are materially inconsistent with the AER's Statement of Expectations and rule requirements
- an assessment of the degree to which the scheme achieved the stated objectives.

The ENA suggested this would provide evidence as to whether the rule change promoted outcomes consistent with the NEO.<sup>81</sup>

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<sup>79</sup> AER, submission to consultation paper, p. 5.

<sup>80</sup> ENA, submission to consultation paper, p. 17.

<sup>81</sup> Ibid.

## G.4 Commission's analysis and conclusions

### BOX 7: FINAL RULE

Eligible retailers will be required to report to the AER on the numbers of customers whose network payments are deferred under the scheme, total network payments deferred under the scheme and the latest due date for payment. The AER will also be required to publicly report on this data each month.

#### **Benefits of final rule**

The reporting requirements under the final rule will provide the market with transparency of the uptake of the deferral mechanism and may help to inform longer-term responses to the COVID-19 pandemic.

The Commission considers there is value in providing transparency to the market regarding the number of customers and quantity of network charges deferred under this mechanism. This rule change introduces a new scheme to assist the retail market in dealing with the unprecedented impacts of COVID-19 and it is therefore important to provide some visibility of:

- the extent to which the rule change is impacting on network businesses
- the extent to which the rule change is helping retailers to manage cashflow problems
- the number of customers that are on the types of arrangements identified in the rule.

Providing for this information to be collected and reported on may also be useful in informing the ongoing response to the longer-term economic impacts of COVID-19.

The final rule requires the AER to report this information to the market each month while the mechanism is in operation. The Commission notes that this aligns with the frequency with which the AER is currently receiving information from retailers on the number of customers on hardship, payment or deferred payment plans. The Commission considers that periodic reporting on the overall use of the scheme will provide valuable data on the level of support that retailers are receiving and how this changes over time.

## H IMPACT ON NSPS

### H.1 Overview

While the deferral mechanism would not reduce the total revenue recoverable by NSPs, it would have an impact on their cash flows in the short-term. This has been an important consideration in the design of the mechanism. The Commission considers it necessary and practical for network businesses to help the market manage the ongoing impacts of COVID-19. However, in doing so the rule change should not impose unmanageable financial risks on networks. These risks can be mitigated through the design of the deferral mechanism.

This appendix discusses stakeholders' views on the potential impact of the rule change on NSPs and how the Commission has addressed these issues through the design of the mechanism.

### H.2 Proponent's views

The AER noted in its submission to the consultation paper that the combination of excluding RoLR retailers and government-owned retailers and imposing interest on deferred network charges will significantly reduce the disruption to network businesses' revenue streams.<sup>82</sup> The AER also noted that the regulatory framework provides significant transparency, predictability and stability for networks and their investors and that network credit ratings have remained stable despite material changes in cash-flow over time.<sup>83</sup>

### H.3 Stakeholder views

Some stakeholders provided feedback and analysis on the potential impacts of the deferral mechanism on network businesses' cash flows, as well as comments on the need for the impacts of COVID-19 to be shared across the electricity supply chain to the extent practicable. Relevant comments are summarised below.

A range of views on the potential impacts on networks were provided in submissions to the consultation paper, with stakeholders noting that this would be highly dependent on the design and scope of the deferral mechanism. Many network businesses therefore advocated for a proportionate and targeted approach when considering the appropriate retailer and customer eligibility requirements.

A number of network businesses commented on the context in which this rule change was proposed, suggesting that networks' revenue streams have already been negatively impacted recently by other regulatory changes and revenue determinations, as well as broader economic conditions.<sup>84</sup> It was noted by some networks that the rule change as proposed by the AER could impose additional cash flow pressure on networks that could pose a material risk to their business. The key risks identified by these stakeholders included:

- networks breaching their debt covenants as a result of the cash flow deferrals

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<sup>82</sup> AER, submission to consultation paper, p. 4.

<sup>83</sup> Ibid.

<sup>84</sup> See for example, submissions to consultation paper, p. ENA, p. 20; Spark Infrastructure, p. 4.

- networks having their credit ratings downgraded
- credit concentration risks for networks at the time when the deferred payments become due.

However, some network businesses considered that the cash flow impacts of the proposed rule change would be manageable and would not introduce a material financial risk.<sup>85</sup> The range of views provided by network businesses likely reflects differences in the preexisting operating conditions and financial metrics of different network businesses operating in the NEM.

The risks identified above were primarily discussed in the context of the proposed design of the deferral mechanism outlined in the AER's rule change request. However, information provided by networks, including analysis provided in confidential submissions, suggested that the cash flow impacts of the deferral mechanism should be manageable for networks if the retailer eligibility criteria excluded large retailers that are not in financial need from accessing the mechanism.<sup>86</sup>

A number of networks also noted that providing for interest to be payable on any deferred network charges would be the preferable method for allowing networks to recover their financing costs, which would further reduce the impact of the rule change on their business.<sup>87</sup>

## H.4

### Commission's analysis and conclusions

The Commission has considered the impact of the rule change on NSPs' cash flows and any associated risks a network business may face as a result. While the final rule will allow some retailers to defer a portion of their network charges for six months, it also imposes a number of limitations that were not included in the AER's proposal which will significantly reduce the financial impact on network businesses.

These elements of the mechanism are discussed in this determination and include:

- the exclusion of RoLR retailers and government-owned retailers (and their related entities) from being eligible to access the deferral mechanism
- large customers (as defined in the NERL, and as applied in each relevant participating jurisdiction) will not be eligible for payment deferrals
- retailers can only defer payment of network charges for residential and small business customers on hardship arrangements, payment plans or deferred debt arrangements
- for any network charges deferred by a retailer, DNSPs will be able to defer the payment of the corresponding TUOS charges. Such payment will include any interest earned by the DNSP on those TUOS charges.
- the payment deferrals only apply to standard control services<sup>88</sup>

<sup>85</sup> See for example, Essential Energy, submission to consultation paper, p. 9.

<sup>86</sup> See for example, SAPN, submission to consultation paper, p. 18.

<sup>87</sup> See for example, ENA, submission to consultation paper, p. 15.

<sup>88</sup> Standard control services are core distribution services associated with the access and supply of electricity to customers.

- the deferrals will only be able to be claimed for a fixed period of six months and will defer payment for a six-month period.
- interest on deferred network charges payable by a retailer is taken to be "billed but unpaid charges" in determining retailer insolvency costs for the purposes of clause 6.6.1(l) of the NER, allowing a DNSP to recover those charges through the existing retailer insolvency cost pass through mechanism.

The Commission also considers that the existing retailer insolvency cost pass through framework in the NER should address some of the concerns expressed by network businesses regarding their ability to recover bad debt in the event a retailer becomes insolvent.

The AEMC has undertaken a high-level assessment of the potential impact of the payment deferrals on the annual revenue for a representative DNSP (taking into account the design elements outlined above). This calculation, set out in Table H.1 below, is driven by simplified and conservative assumptions based on publicly available data and so should only be used as an indicative assessment.

**Table H.1: Estimated impact of deferral mechanism on representative NSW DNSP's annual revenue**

DESIGN ELEMENT	REDUCTION IN SHARE OF ANNUAL REVENUE IMPACT-ED	TOTAL ANNUAL REVENUE IMPACT-ED	SOURCE
Six-month deferral period	50%	50%	Assuming flat consumption across the year
RoLRs and government-owned retailers ineligible for payment deferrals	88% (of 50%)	6%	Market shares of these retailers for NSW (based on AER retail statistics)
Large customers ineligible for payment deferrals	10% (of 6%)	5.4%	Estimated large customer share of network revenue
Payment deferrals only for customers of eligible retailers on hardship arrangements, payment plans and deferred debt arrangements	90% (of 5.4%)	<1%	Upper estimate of 10% of eligible retailers' customers meeting these criteria based on AER retailer data dashboard (29 June 2020)
<b>Estimated share of</b>		<b>&lt;1%</b>	

DESIGN ELEMENT	REDUCTION IN SHARE OF ANNUAL REVENUE IMPACT- ED	TOTAL ANNUAL REVENUE IMPACT- ED	SOURCE
<i><b>total annual DNSP revenue deferred</b></i>			

Source: AEMC

Table H.1 shows that the estimated impact of the deferral mechanism on a representative DNSP in New South Wales is expected to be less than one per cent of that DNSP's annual revenue. The Commission acknowledges that this amount will vary for each DNSP and may be higher for DNSPs operating in distribution areas where the retailers excluded from the deferral mechanism have a smaller market share and/or eligible retailers have a higher proportion of customers on payment plans, hardship arrangements or deferred debt arrangements. However, the Commission considers that this analysis illustrates that the impacts of a deferral mechanism with the limitations imposed under the final rule should not present a material financial risk for DNSPs. This analysis is also consistent with feedback provided by network businesses in submissions to the consultation paper.

The combination of the eligibility criteria discussed above and the imposition of interest on deferred network charges means that the final rule should not result in a material change to NSPs' overall risk profile. Accordingly, the Commission does not consider that the effect of the deferral mechanism should be considered in future determinations of NSPs' WACC.

# I SUMMARY OF OTHER ISSUES RAISED IN SUBMISSIONS

This appendix sets out the issues raised in the first round of consultation on this rule change request and the AEMC's response to each issue. If an issue raised in a submission has been discussed in the main body of this document, it has not been included in this table. The table does not include issues raised in submissions to the directions paper.

**Table I.1:** Summary of other issues raised in submissions to consultation paper

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
<b>RoLR framework</b>	ENA, p. 9	If there are significant concerns about the capacity and operation of the RoLR scheme, it should be subject to a comprehensive review or the COAG Energy Council should implement the recommendations of the NEM financial market resilience review.	Changes to the RoLR framework are outside of the scope of this rule change.  The Commission's 2020 Retail Energy Competition Review made a number of recommendations to enhance the resilience of the retail energy market, including changes to the RoLR framework. These recommendations build on the work undertaken for the Commission's 2015 NEM financial resilience review.
<b>Interaction with other reforms</b>	ENA, p. 9	The Commission's decisions on the requirement for, and scope of, any rule change need to be undertaken with a clear and prospective view of the range of other direct policy interventions that are likely to impact on the need to undertake a rapid and unprecedented reassignment of	The Commission has considered the interaction between various regulatory reforms and support measures as part of its policy development process. Ongoing reforms will also need to consider their interaction with this final rule.



ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		cashflow risk from one part of the energy supply chain to another, with all consequent risks this step would potentially entail.	
<b>Impact on prices</b>	ENA, p. 10	<p>There are critical potential impacts of the proposed rule change arising from this forced loan provision that go directly to the long-term interests of customers which are not sufficiently examined or considered in the original proposal. These need to be fully evaluated in the Commission's review process.</p> <p>These are:</p> <ul style="list-style-type: none"> <li>Shifting cashflow risk may result in customers just paying more – If the AER rule change leads to higher debt costs or charges, to underwrite the participation of retailers that may fail shortly after the expiry of the deferral period, there is a risk of current and future customers paying more for no net benefit.</li> </ul>	<p>The Commission does not consider that the rule change should result in higher prices for customers. The final rule allows network businesses to recover their full regulated revenue, while also reimbursing them for the borrowing costs they may incur through the imposition of interest on deferred network charges. Further, the limitations on retailer and customer eligibility under the final rule significantly reduce the financial burden on network businesses. As discussed in appendix h, the Commission estimates that payment deferrals are likely to impact on less than one per cent of a DNSP's annual revenue. Feedback from NSPs largely supports the view that the impacts of the deferral mechanism as set out in the final rule will be manageable.</p>

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		<ul style="list-style-type: none"> <li>Shifting cashflow risk does not necessarily result in an offsetting customer benefit – Meeting the objective of keeping prices at the lowest sustainable levels over time for customers it is not simply a question of reducing risk for operators in competitive retail markets. Rather, it is equally critical that electricity distribution and transmission companies are liquid and able to stably maintain benchmark credit metrics. Customer reap tangible cost benefits from financial stability across the whole electricity supply chain.</li> </ul> <p>The rule change proposal accepts that customers are likely to ultimately meet the cost of this direct shift along the supply chain of retailer cashflow risk.</p>	
<b>Cost-benefit analysis</b>	ENA, p. 10	Establishing this proposition in the current circumstances would appear to require an empirical	In considering any rule change request, the Commission considers whether the change is in the long term interests of consumers. The

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		assessment of the benefits of a competitive retail market 'with and without' the policy intervention proposed. This assessment should be undertaken to ensure clear customer benefit delivered from any rule change.	Commission considers that the final rule is likely to be in the long-term interests of consumers for the reasons set out in chapter 3. A cost benefit assessment would not be able to robustly or comprehensively quantify the net benefits of the mechanism.  It is also difficult to directly attribute incremental costs of implementing a change to the regulatory framework to a particular rule change at a time when there are numerous changes underway and the economic situation surrounding the COVID-19 pandemic is continually evolving. However, the Commission has undertaken high level analysis of the potential impact of the rule change on DNSPs, which has informed the Commission's decision making in addition to the qualitative assessment set out in chapter 3 of this determination.
	Spark Infrastructure, p. 1	We are deeply concerned that the assumed additional benefit of deferring the network component of a customer bill, over and above the support provided by governments to businesses and individuals and the RoLR scheme, do not outweigh the cost.	
<b>Obligations relating to customer disconnection</b>	ENA, p. 10	Consideration should be given to how legal obligations can be placed on retailers to not disconnect residential and small business customers for the period for which the final rule applies. At the minimum, the AER's	As discussed in the body of this final determination, the obligation on retailers under the AER's Statement of Expectations not to disconnect residential and small business customers has been extended to 31 October 2020 (and potentially beyond). The Commission considers that imposing an

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		Statement of Expectations with regards to retailer disconnections should be extended for the period for which the final rule applies.	equivalent legal obligation on retailers under the rules could have unintended consequences and the AER is best placed to monitor compliance with the Statement of Expectations.
	Endeavour Energy, p. 9	If the AEMC considers a rule change is necessary, it should consider whether the requirements of the Statement of Expectations should instead be made legally binding obligations in the rules. Otherwise, the rule change will place binding obligations on network businesses to support retailers whilst retailers would not have equivalent obligations to support residential and small business customers.	
<b>Purpose of deferral mechanism</b>	SAPN, p. 4	If the proposed deferral mechanism is implemented, it should only operate as a last resort to maintain a retailer's financial viability and should only apply to the extent that a retailer requires assistance above and beyond the extensive measures and support that are, and become, available.	The Commission considers that the requirements imposed on retailers that seek to defer the payment of network charges under the final rule, particularly the imposition of interest on deferred charges, should incentivise eligible retailers to explore alternative options to manage any cash flow issues before resorting to the deferral mechanism.

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
	Red and Lumo, p. 2	<p>A further issue for the Commission's careful consideration is the incentive that any deferral could create for retailers to avoid more fundamental changes to their business model to maintain their financial viability and to limit their exposure to future economic downturns.</p> <p>Retailers must act in an economically rational manner, and should seek additional finance from a bank, equity from shareholders or renegotiate contracts with counterparties (such as generators and large customers).</p>	
<b>Additional support for retailers</b>	AEC, p. 3	<p>The AER's proposed rule change only considers cash flow risk – it does nothing to mitigate upstream costs, or reduce non-payment caused by interventions in the retail market. In effect, unless a customer who doesn't pay immediately pays before 31 December, the proposed rule</p>	<p>The purpose of this rule change is to establish a limited mechanism to assist retailers in dealing with the immediate cash flow impacts of COVID-19. The rule change has been progressed as an urgent rule in an expedited timeframe in order to achieve this objective.</p> <p>The Commission has set out its consideration that bad debt risk is generally most efficiently allocated to retailers. Further, the Commission</p>

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		<p>change will not provide any benefit to a retailer unable to meet its obligations to the market. In short, it is likely the retailer who could not pay its debts before 31 December 2020, will still not be able to pay those debts after 1 January 2021. In this scenario, the rule change could be considered to only mitigate the risk of RoLR events in 2020 – it does nothing to avoid them in the future.</p> <p>To that end, if a retailer is cash poor, the rule change might enable them to continue to function long enough to repair its liquidity to a manageable level. For all other retailers, the rule change is likely to be of little long-term benefit.</p>	<p>considers that there would be significant complexity involved in considering whether networks should be required to share the risk of bad debt with retailers and how this would need to be dealt with in the regulatory framework.</p> <p>The Commission also notes that if a significant change to the normal allocation of risk in the NEM is necessary to help retailers manage the impacts of COVID-19 (which is not clear from the evidence available at this time), it may be appropriate to consider further rule changes or other policy measures to address this issue. The Commission considered these issues within the 2020 Retail Energy Competition Review.</p>

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
	AGL, p. 1	The rule provides cashflow relief for retail customers that have taken out a payment plan to manage their energy bills during the pandemic. The rule does not address the impact on retailer bad and doubtful debts generated by many of these customers and that are under financial stress due to COVID-19. Further, the rule does not address likely retailer debt impacts from customers under financial distress who have opted to defer their electricity payments. For example, AGL's COVID-19 Customer Support Program allows AGL residential and SME customers impacted by COVID-19 to defer electricity payments until 31 July 2020. Lastly, the rule does not address the impact on retailer bad and doubtful debts generated by many retail customers under financial stress due to COVID-19 who have not actively engaged or sought a payment plan.	
	Alinta Energy, p. 1	Whilst the rule change may reduce	

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		the immediate likelihood of retailer failure, it will not, of itself, prevent a retailer of last resort event occurring, and there is a danger that any broader impact on the retail energy market may be compounded at the end of the rule change period. An alternative approach would be for network businesses to cover a set proportion of the debt write-off provided by retailers to their customers.	
	Alinta Energy, p. 2	We believe there is an opportunity to examine additional or alternative mechanisms to minimise the risk of retailer failure. Changes to the determination and application of the DMO is one such opportunity, where an allowance for costs beyond the control of retailers could be included. Such changes would impose limited cost on the economy, but would contribute to the ongoing viability of retail competition in the energy sector.	



ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		There is also an opportunity for broader consideration of the extent to which network businesses should share some of the ongoing customer credit risk, given the restrictions on the ability of retailers to directly manage that risk due to imposition of the DMO and VDO, and other regulatory changes impacting the credit collection process.	
	amaysim, p. 2	<p>amaysim is supportive of the Rule Change and suggests the following enhancements to the Rule Change proposal:</p> <ul style="list-style-type: none"> <li>• widening the criteria of the Rule Change to include customer arrears incurred by retailers as a result of COVID–19. It is these arrears that will impact upon bad and doubtful debts for retailers. These debts are not currently captured by the Rule Change; and</li> <li>• expanding the definitions and eligibility within the proposed Rule Change to capture a broader</li> </ul>	

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		segment of customers who are unable to pay their bills.	
	ERM Power, p. 1	Although the proposed rule change provides welcome cashflow relief so retailers can continue to extend payment plans for energy consumers in financial difficulty, it does not contemplate networks (or generators) sharing the burden of bad debts. We are supportive of the cash flow relief proposed but consider that the mechanism should also cover the sharing of bad debt.	
	Origin Energy, p. 1	The rule change proposes to support the financial resilience of the energy industry by reducing the cash flow pressures on retailers through deferred network payment arrangements. These network payments will nevertheless remain a future liability for retailers. However, we believe the greater risk to retailer failures relates to any potential material change in bad and doubtful debts because retailers	

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		may not recover enough future payments from their customers to remain viable.	
Other	SAPN, p. 4	If the AEMC forms the view that there is a further need for the cash flow impact of COVID-19 to be shared with electricity network businesses, then other parts of the supply chain should also be considered.	The Commission considers that providing for some of the immediate cash flow risks associated with COVID-19 to be shared between retailers and networks is the most efficient and practical approach to provide some cash flow relief to retailers during this period. As regulated monopolies with guaranteed revenue allowances, networks are well placed to bear some of the cash flow burden and are likely to be able to access additional credit to cover any deferred cash flows if necessary. In addition, it is likely to be complex, impractical and highly disruptive to the wholesale market to allow retailers to defer the payment of wholesale electricity costs in addition to network charges. As such, the Commission has not considered this as a viable option through this rule change process.
	SAPN, p. 14	The wording of the Proposed Rule Change reflects that the deferral period of 6 months is absolute, yet retailers may well receive payments under a payment plan during that period. It is	The Commission acknowledges this concern, however it is unlikely that the scenario described could be easily dealt with in the rules. This is in part due to differences in DNSP-retailer and retailer-customer billing periods. In addition, even where customers on

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		<p>unreasonable to allow a retailer to retain the full benefit of any payments it receives from a customer during that time and not pass through to electricity networks at least a portion of the amounts received.</p> <p>The proposed deferral mechanism should only apply to the extent that an eligible customer has not paid any portion of the network charges that are payable by the customer during the deferral period. If, at any time during that period, that customer makes any payment, the retailer should be required to pass through to electricity network businesses the portion of that payment that can be attributed to network charges.</p>	<p>payment plans and hardship arrangements are able to make some payment to the retailer, it may be substantially less than what is owed. In any case, the final rule does not prevent retailers from repaying deferred network charges before the due date and retailers may elect to do so to avoid additional interest charges. The Commission considers that retailers and network businesses should be able to resolve this issue through negotiation. This scenario could also potentially be dealt with through the implementation processes participants are required to agree on and implement.</p>
	PIAC, p. 1	<p>In PIAC's view the number of retailers currently in the market has not brought a diversity of offerings to energy consumers, has not resulted in efficient and fair prices for many energy</p>	<p>The preservation of existing levels of market competition is not the sole purpose of this rule change. However, the Commission does consider that the exit of multiple retailers from the market as a result of COVID-19 and altered regulatory obligations would likely lead</p>

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		consumers, and has not effectively spread risk. Some retailers were failing to meet their minimum requirements for hardship customers and disconnections prior to the pandemic. In light of this, PIAC does not consider preserving the existing level of retail competition an end in itself, nor the avoidance of triggering Retailer of Last Resort.	to outcomes that are not in the long term interests of consumers. As such, this is a relevant consideration when considering whether the rule change meets the NEO.
	Ausgrid, p. 7	<p>In the AER rule change proposal and the AEMC consultation paper, neither the AER or AEMC have identified where the network businesses will quickly access funds from, should they be required. However, there seems to be a view that network businesses are not subject to liquidity risk and have cash 'on tap' whenever they want it.</p> <p>Network businesses are subject to the same constraints as other firms when it comes to accessing funds. These constraints are likely</p>	The Commission acknowledges that network businesses are subject to liquidity risk. However, as regulated monopolies, networks are likely to be able to borrow funds more easily than many other market participants, particularly during this period of market volatility. The Commission has also sought to limit the impacts on networks through the retailer and customer eligibility criteria. The Commission therefore considers that, having regard to the limitations imposed on the deferral mechanism under the final rule, a benchmark efficient network business should be in a position to access the funds required to account for the deferred cash flows they may experience.

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		to be more acute during times of market volatility, such as the present circumstances.	
	ECA, pp. 3-4	<p>This rule change must be backed-up by a coordinated and well-funded, public awareness campaign to ensure that consumers know that assistance is available and know how to get it. This is because in surveys we commissioned to better understand how consumers were being impacted by COVID19, we found that electricity bills are the bills that people have the most concerns about being able to pay</p> <p>...</p> <p>We also see a role for government to complement outreach by energy companies, by using platforms like the COVID-19 app and advertising to promote trusted information. The Australian Government invested in an advertising campaign to increase the uptake of the COVID-19</p>	The Commission agrees with this comment, however this is outside the scope of this rule change.

ISSUE	STAKEHOLDER	COMMENT	AEMC RESPONSE
		tracing app. To make sure people get access to the assistance they need so they can keep the power on, and stay warm this winter, governments should do the same in relation to awareness around the availability of energy bill support.	
	Energy Queensland, p. 2	Should the AEMC decide to introduce this proposed rule change, we suggest the AEMC consider the possibility that a retailer who is eligible to defer network charges may become insolvent or fail before these charges have been repaid.	The Commission has considered this scenario in its assessment of the rule change. Should a retailer become insolvent before deferred network charges have been paid by that retailer, the DNSP would be able to recover those charges through the existing retailer insolvency cost pass through mechanism.
	EnergyAustralia, p. 4	We believe that measures to support retailers should not be limited to electricity, and that the AEMC should consider expanding the rule to cover gas networks.	The AER's rule change request proposed changes to the NER to deal with the impacts of COVID-19 on the retail electricity market. Expanding the AER's proposal to include changes to the National Gas Rules would be beyond the scope of this rule change.