

# Electricity Networks Association

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Retail Advisory Group  
c/o Electricity Authority  
Level 7, ASB Bank Tower  
2 Hunter St  
Wellington

Dear Retail Advisory Group

## Submission on Retailer Default Discussion Paper

We refer to your Discussion Paper "*Arrangements for Managing Retailer Default Situations*" of 14 August 2012. The Electricity Networks Association (ENA) supports the approach to managing retailer default situations proposed in this Discussion Paper. In particular, the ENA supports this proposed retailer default process as it:

- Utilises commercial mechanisms as far as practical to address a retailer default event;
- Does not rely on disconnecting consumers (as we would be concerned with the disruption to consumers from any process that placed a heavy reliance on disconnecting); and
- Includes in the definition of a "default event" default by a retailer on certain obligations to a distributor pursuant to a Use of System Agreement (UoSA).

However, ENA is concerned that the prudential requirements on retailers allowed for under the Code in relation to UoSAs are neither consistent with the time periods in the proposed approach nor consistent with the prudential requirements in the wholesale electricity market. ENA notes that the Electricity Authority (EA) has not made transparent the information or analysis provided by the Commerce Commission that purports there is some coverage for default risk in the calculated WACC. The existing prudential requirements in the Code and the time periods envisaged under the proposed retailer default process would result in electricity distribution businesses (EDB) being exposed to bad debts of around 60 trading days<sup>1</sup> worth of service in the event of a retailer default.

By way of context, in October 2011 the EA shortened the period of cover for prudential requirements in the model UoSAs from two months to 14 days, and made this shorter period a mandatory cap by way of the Code.<sup>2</sup> Given that the EA has chosen to regulate this aspect

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<sup>1</sup> This is derived from up to 77 days of trading at risk (see below), less the 14 days prudential cover, equalling 63 days.

<sup>2</sup> See clause 12A.4 of the Code. In addition to requiring security to be posted for defined periods the Code allows for certain credit ratings (e.g. BBB-) to qualify for prudential requirements. These new

of an EDB's business, the ENA considers the EA and Commerce Commission jointly need to ensure this regulated cap on prudential requirements is consistent with the time period envisaged in the proposed retailer default process and the WACC calculated for EDBs. We note that, when the Commerce Commission determined the WACC, at the time the prudential security allowances covered two months of trading.

The ENA recognises that it is impractical to shorten the time periods in the proposed retailer default process. The ENA considers that the Authority and Commerce Commission should revisit the appropriate remedy to this mismatch in time periods either by considering an extension to the prudential requirements allowed for under the Code for UoSAs to cover the period to complete the retailer default process in an expeditious manner; or by increasing the WACC to explicitly account for default risk; or providing for this risk through a specific self-insurance cost that could be recovered under the regulated price path. Taking the approach proposed in the Discussion Paper, and assuming payment on the 20<sup>th</sup> of the month following supply of the distribution service, the overall approach needs to be reflect that the values at risk cover:

- 30 or 31 days of service provided in the previous month, plus 20 days to the 20<sup>th</sup> (up to 51 days);
- Plus the time to either resolve the default issue or transfer consumers to a new retailer by way of a sale. The Discussion Paper indicates this step would take a minimum of 8 working days (a total of 12 days if these days span two weekends);
- Plus the time taken for the EA to notify any remaining consumers their retailer is in default and that they need to transfer to another retailer, for which the Discussion Paper allows 10 working days (a total of 14 days if they span two weekends); and
- In sum this suggests prudential cover needs to provide for a period of up to 77 days (31+20+12+14).

It is easy to imagine that the process envisaged under the proposed retailer default process may for practical reasons take longer than hoped for in the Discussion Paper.

The ENA notes the extensive modelling and analysis undertaken by the Wholesale Advisory Group to develop prudential requirements for the wholesale market and submits that no lesser analysis should be undertaken by the EA and Commerce Commission in developing the most appropriate approach, recognising that the EA has a specific interest in ensuring that there are not undue barriers to entry for new retailers. The ENA requests the Retail Advisory Group (RAG) raises this need to review the prudential requirements related to UoSAs and/or Commerce Commission arrangements in its recommendations on addressing retailer default.

The RAG seeks comment on the scope of the EA's involvement in addressing situations where a retailer has defaulted to an EDB. The ENA submits that EDBs should be entitled to call upon the EA's involvement in certain circumstances in order to ensure the orderly transfer of consumers to traders entitled to trade on a distributor's network when a retailer's contract with the EDB has been terminated. These circumstances should include:

1. The retailer is no longer entitled to trade on the network;
2. There are no unresolved disputes between the retailer and the distributor relating to the termination; and
3. The retailer has not taken timely steps to arrange for consumers to switch to another valid retailer, or its consumers have refused to switch.

Such an approach would protect retailers' reasonable commercial interests and ensure EDBs are not left in an invidious position where the only option available to them is to disconnect consumers in order to effect a switching of consumers to valid retailers (i.e. those with a UoSA). The ENA submits that the option of seeking the EA's assistance should not be restricted to situations of financial default, as there are other legitimate reasons where a UoSA may be terminated (e.g. a retailer has failed to perform other duties required under the UoSA such as systematically not supplying accurate data for billing purposes).

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Alan Jenkins', with a long horizontal flourish extending to the right.

Alan Jenkins  
Chief Executive  
Electricity Networks Association