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Retail Advisory Group
c/o Electricity Authority
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Discussion Paper: Arrangements for managing retailer default situations

Introduction

Mighty River Power (MRP) welcomes the opportunity to respond to the Retail Advisory Group (RAG)'s Discussion Paper: "*Arrangements for managing retailer default situations*", dated 14 August 2012. No part of the submission is confidential and we are happy for it to be made publicly available.

Comments

As stated in our previous submission on this issue, MRP considers that the risk of retailer default resulting in unallocated customers is low. History suggests that the customer portfolio of a failed retailer will probably be transferred to an alternate retailer via some commercial arrangement without the need for intervention.

However, MRP accepts that there is merit in putting in place backstop arrangements provided that the arrangements are workable and the costs do not outweigh the benefits. Under current Code provisions, in the unlikely event that a retailer is in default and no commercial solution eventuates the Clearing Manager is unable to transfer a defaulting Retailers' customer base to solvent retailers yet generators and network companies will continue to bear the costs until the defaults are remedied or relevant customers transferred.

The latest consultation paper provides for a broadening of the “events of default” to include a defaulting retailer’s failure to pay lines charges under its bilateral contracts with distributors. We have no particular problem with these proposals.

The paper provides for a two stage process whereby the defaulting retailer is given a week to transfer its customers to a solvent retailer, failing which the Electricity Authority (Authority) will advise customers of the default and request them to switch to another retailer within a specified time period. Any customers who do not do this could be transferred using one of three methods;

- Mandatory pro-rating of customers across all retailers on each network,
- by a competitive tender process; or
- Mandatory allocation of customers in each network to the largest retailer operating on that network.

All these options will impose a degree of cost on solvent retailers. These costs must be balanced against those associated with allowing the default to remain unresolved, the costs of which are borne by generators and networks. We prefer the first option on the basis that it is likely to be the simplest and quickest method of transferring the remaining small pool of customers to a solvent retailer. However, we believe it should be amended to include allocation only to those retailers who currently serve the market segment (e.g. residential, small commercial etc, on the network and only those who have generally more than 10% market share of that segment on the network. This is to avoid cost and complication for retailers.

The proposals involve giving the Authority a range of new powers. We look forward to having the opportunity to comment on any draft Code amendments if the Authority decides to proceed with the proposals. We also look forward to full disclosure of any legal advice that is material to the drafting of the Code provisions, in particular around the issue of ensuring that there are no confusing overlaps between the powers of the Authority and any receiver appointed to a retailer and any new obligations on retailers to be included in contracts with customers.

The proposals are predicated on a set of timeframes for managing a retailer default. These timeframes are critical as they directly affect the length of time generators and networks will continue to bear the costs until the defaults are remedied or relevant customers are transferred. The timeframes have been subject to stress testing. The feedback given to the Authority was that some of the timeframes, for example, the requirement to send letters to thousands of customers of the defaulting retailer and expecting them to react within 10 days is ambitious. We understand the intent of these timeframes but suggest that the Authority may wish to reserve its right to approve on extension of component parts of them, where

such an extension would be reasonable in the circumstances and is in the balanced best interest of all parties.

Should you have any queries in relation to any of the above or other related issues please do not hesitate to contact me on 09 580 3734 or Nigel.Williams@mightyriver.co.nz

Yours sincerely

A handwritten signature in black ink, appearing to read 'Nigel Williams', with a horizontal line extending from the end of the signature.

Nigel Williams

Manager Operations

QUESTION	COMMENT
<p>1 Do you agree with the summary of the options available to a distributor in the event of a default by a retailer, or are there other remedies available to a distributor?</p>	<p>This is a reasonable summary that captures the main elements of available options. We do believe that additional lessons could be learnt from the recent E-gas experience and the legal parameters between the Authority and retailers need to be clearly established.</p>
<p>2 Do you consider that a distributor could be sufficiently concerned about the prospect of a default by a retailer to insist on a conveyance use-of-system agreement for the use by retailers of its network, and if so, would this be an undesirable outcome?</p>	<p>Yes, it is an undesirable outcome</p>
<p>3 Should a distributor, after terminating a use-of-system agreement with a retailer as a result of an unresolved serious financial breach by that retailer, have an option of advising the Authority that it considers an event of default exists and that this event should be subject to the proposed arrangements under the Code to manage an event of default?</p>	<p>In principle yes as long as the Authority has the power to do so, and if it makes a thorough assessment of the validity of the claim by the distributor.</p>
<p>4 Are there any other events not currently captured by clause 14.55 that should be defined as an event of default and if so on what rationale?</p>	<p>No</p>
<p>5 Should the Code provisions governing the notification of a default be broadened to require all participants and service providers to notify the Authority as soon as that entity has reasonable grounds to believe that an event of default is likely to occur, or has occurred?</p>	<p>Yes, it promotes good industry practice.</p>

QUESTION	COMMENT
<p>6 Should the clearing manager have an obligation to advise an entity if it has not complied with a requirement of Part 14 of the Code and that this non-compliance is an event of default?</p>	<p>Yes, as Rule 14.57 stipulates, the Clearing Manager needs to notify the entity and has to refer the issue concerning an event of default to the Authority.</p>
<p>7 Should the Code be clarified and simplified by bringing the actions that may be taken by the clearing manager in the event of a default into one sub-part and re-drafted to stipulate, to the extent practical, the actions the clearing manager would take in relation to a shortfall in payment or a failure to meet a call?</p>	<p>Yes</p>
<p>8 Should the Code stipulate that on being notified of an event of default, the Authority would immediately investigate and determine: a. whether an event of default exists; and b. if an event does exist whether that event is a minimal risk event arising from a technical or administrative failure that has or will be corrected within one business day or a commercial disagreement that doesn't affect the retailer's long-term ability to trade?</p>	<p>Yes, with respect to (a), we believe that it is a necessity to investigate whether an event of default exists.</p> <p>With respect to (b) we do not see any value in unnecessarily causing distress within the Industry. We fail to understand the importance of minimal risk event that does not affect the retailer's long-term ability to trade. Questions arise as examples,</p> <ul style="list-style-type: none"> • "Will this data be recorded on a database to monitor retailer trends, • how will the reporting of this data be structured, • and who the audience will be. <p>Overall the codification of event defaults levels would provide greater clarity as to the process that will follow an event of default.</p>

QUESTION	COMMENT
<p>9</p> <p>Should any assessment by the Authority of whether the event is a minimal risk include a materiality threshold, equivalent to the serious financial breach threshold under the draft model use-of-system agreement?</p>	<p>Yes, but we are not convinced that a financial breach threshold should be the sole determinant, there may be other factors that should be taken into account. As stated in response to Q8 we propose that minimal risk events that do not have an effect on the retailer's long-term ability to trade, not be reported on, and be used for the Authority's confidential use only.</p>
<p>10</p> <p>If distributors are provided with an option of notifying the Authority that they had terminated a retailer's use-of-system agreement as a result of an unresolved serious financial breach, should the Authority be tasked with assessing whether the distributor had complied with the notice terms of the use-of-system agreement and, in the absence of action by the Authority, would be entitled to notify consumers that they would be disconnected unless they switched to an alternative retailer?</p>	<p>Yes</p>
<p>11</p> <p>Should the Code stipulate that on determining that an event of default of more than minimal risk exists the Authority would advise the retailer and its agent(s) that unless the default is rectified within a specified number of days, the Authority would: a. communicate with all of the retailer's customers advising them that their retailer had defaulted and that the customer should switch to another retailer and that if they did not switch by a specified date the Authority would assign them to another retailer; and b. proceed to terminate the retailer's rights to trade electricity under the Code?</p>	<p>Yes, subject to what the proposed timeframes are- (see covering letter).</p>

QUESTION	COMMENT
12 Should the Code require that retailers include an assignment clause in their customer contracts?	Yes
13 What period of time, measured in days, is necessary to allow sufficient time for a retailer to transfer responsibility for its customers to another retailer or to rectify the default?	A suitable timeframe needs to be established even if it is an estimate at this stage.
14 Should the relevant period of time be specified in working days or in calendar days?	Working days, as this is standard industry practice.
15 Should a mechanism exist to extend the number of days provided to the retailer in default to rectify the event of default, including any interest payable, if that extension of time is approved by the parties who would bear the financial risk of an extended time period?	Yes - provided affected parties (those that will bear the financial risk) are consulted.
16 Should any extension of time for rectifying the default require approval of a majority in number representing 75% in value of the money owed or some other threshold?	Yes, The represented percentile (75%) seems to be in accordance with section 228 of the Companies Act. Our view is that no change needs to be effected as it may create complexity and confusion.
17 Should the Code provisions that provide for generators to be assigned or subrogated to the rights of the clearing manager be removed from Part 14?	Yes, Part 14 rules need to be reviewed and altered to reflect the functions of the Clearing Manager.

QUESTION	COMMENT
<p>18 If, at the end of the eight-day period, the defaulting retailer has not satisfied the Authority that it (the retailer) is no longer in default, or has not transferred all of its customers to another retailer, should the Authority have the ability to communicate with the retailer's customers advising those customers that their retailer had defaulted, that they should switch to another retailer and, that if they did not switch by a specified date, the Authority would arrange for them to be transferred to another retailer?</p>	<p>Yes, the remaining retailers need to be informed. Additionally with the Authority facilitating this process it should be able to justify to external parties and clarify to these parties the process from origin (defaulting retailer not satisfying the Authority after the eight-day period) until conclusion.</p>
<p>19 Should the Authority be able to facilitate this voluntary transfer by providing the customer list of the retailer in default to competing retailers so that they may make their own approaches to the customers of the retailer in default?</p>	<p>Yes, the Authority is best placed to facilitate this voluntary transfer. This process would need to be defined and agreed upon by all parties, but we fail to see how this is any different across for the ability of the receiver to make the necessary arrangements.</p>
<p>20 What period of time, measured in days, should be provided by the Authority to the customer of the retailer in default to voluntarily switch to an alternative retailer?</p>	<p>10 business days to complete all switching will likely be unachievable. Some days are required for the consumer to act, plus mail time and switch processing times, However, if the intent is to drive rapid action by the customer and the Authority is likely to extend the timeline (not publicly) in practice, then 10 days would seem appropriate.</p>
<p>21 Should the Code impose on retailers an obligation to have the following provisions in their contracts: a. in a default situation, the Authority may terminate the contract between the retailer and its customer; and b. if the Authority terminates the contract under (a), the customer would become bound by a contract with another retailer stipulated by the Authority?</p>	<p>We believe that this will not be necessary on top of the assignment clause, and careful consideration should be given to the cost versus benefits of such an option.</p>

QUESTION	COMMENT
<p>22 Should retailers in the same network area be required by the Code to enter into contracts with customers of the defaulting retailer whose contracts have been terminated by the Authority?</p>	<p>We do not believe that this is necessary or appropriate and it subverts the retailer's normal business practice and decision making. All retailers should be considered and included as some might be looking to progress into particular areas. With this neutral approach the Authority cannot be accused of preferential treatment and customers will have an opportunity to switch within the allocated timeframe.</p>
<p>23 Should the Code provide for the Authority to invite other retailers to tender to provide contracts to the customers of the failed retailer whose contracts the Authority has terminated?</p>	<p>No, as this is the responsibility of the receiver.</p>
<p>24 Should the Code enable the Authority to allocate, as a last resort, any remaining customers of the retailer in default amongst retailers on the affected network on a pro rata basis based on a historic retail volume measure?</p>	<p>Yes, while this is not an ideal approach we consider this to be the best available approach under the circumstances. However, the Authority should take into account the types of customers retailers have, residential, commercial, electricity, gas, time of use, etc. and the scale (and ability to cope) of the receiving retailers activity in the network (See covering letter) Not all retailers offer all these services.</p>
<p>25 If you do not agree with a pro rata basis, what method should the Authority use to allocate any remaining customers of the retailer in default amongst retailers on the affected network?</p>	<p>We support the pro-rata basis, subject to the scale caveat in our cover letter.</p>
<p>26 Should responsibility for the customer, caused to be transferred by Authority, change to the new retailer on the date of the switch?</p>	<p>Yes, legally the retailer is responsible for the property on the date of the switch.</p>

QUESTION	COMMENT
<p>27 Should the Code be amended to require a retailer in default to provide the Authority with the information it would need to write to all of the retailer's customers advising them that the retailer is in default, and if necessary, to cause any remaining customers to transfer to another retailer?</p>	<p>Yes we believe it should be amended to require a retailer in default to provide the Authority with access to a fully detailed customer list. Furthermore we would suggest that a medically dependant list be provided first to ensure that medically dependant customers are primarily supported without any disturbance.</p>
<p>28 Do you agree that to address the potential for information difficulties the Code should provide for the Authority to: a. advertise to advise customers of the retailer in default that they should choose an alternative retailer; b. access information held by the Registry and distribution utilities to reconstruct a customer database if necessary; and c. instruct the Registry to act as counterparty for customers switching voluntarily from the retailer in default, if required?</p>	<p>a. Yes b. Yes. c. If required, yes</p>