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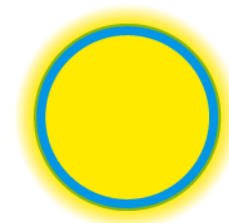
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POWERCO



Dear Carl

Powerco submission on arrangements to manage a retailer default situation

1. Powerco Limited (Powerco) welcomes the opportunity to comment on the consultation paper *Arrangements to manage a retailer default situation*, published by the Electricity Authority (Authority) on 18 June 2013.
2. This submission comprises:
 - general comments relevant to the paper; and
 - responses to the RAG's detailed questions (Appendix A).
3. Powerco supports work that contributes to reducing potential disruption of supply to customers and maintaining confidence in the market. It is important for the industry that there be a high degree of certainty around the process that will be followed after the failure of a retailer. All participants in the supply chain (including customers) would benefit from an improvement to the existing situation, as the current lack of a backstop arrangement means that, at present, insolvency of a retailer would leave all the parties involved exposed to a significant degree of risk for an indeterminate amount of time. Notably, consumers can currently be left connected and consuming electricity, but with no retailer.
4. This consultation represents a positive step forward by setting out proposed Code amendments that would allow the Authority to take effective action on an issue that has not been adequately addressed since the New Zealand Electricity Market (NZEM) rules transitioned to the Code.
5. Powerco is pleased that the Authority has recognised the significant financial risk that generators and distributors would face if a lengthy resolution process were to follow a retailer default. The proposed 17 elapsed days strikes a reasonable balance that limits financial exposure while also providing adequate time to complete the necessary commercial transactions.
6. We believe that a simple and clear process, requiring several steps to be completed within tight but realistic timeframes will, when combined with normal commercial

incentives, be the best way to limit the risk of cascade failure. For this reason, we do not believe that introducing a tender process for any unallocated customers would improve the overall arrangements for managing a default event, due to the additional complexity it would create. We anticipate that consumers will understand the need to switch retailers from the Authority's communications, and those retailers that would benefit commercially from acquiring new customers aggressively pursue those consumers. Consequently, we believe that, at that stage in the process, the market should be allowed to operate without further intervention.

7. We have reviewed the drafting of the proposed amendment and, on the whole, are satisfied that it reflects the intent of the proposal. However, we are seeking further clarification of the meaning and purpose of two of the proposed clauses (11.15A.1(c) and 14.55(h)(iii)). Please feel free to contact us if you would like to discuss our concerns about the drafting of these two clauses.
8. Thank you for the opportunity to make this submission. If the Authority wishes to discuss any aspects of this submission, please contact Oliver Vincent, oliver.vincent@powerco.co.nz , ph. (06)757-3397, in the first instance.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Richard Fletcher', with a stylized flourish at the end.

Richard Fletcher
General Manager Regulation and Government Relations

Appendix A: Responses to the consultation questions

	Question	Powerco Response
1	Has there been any development since submissions were received on the problem definition developed by the RAG that might warrant the Authority reconsidering its view as to the nature of the problem?	No.
2	Do you agree with the objectives of the proposed amendment? If not, why not?	Yes. Amending the Code to achieve the stated objectives will address the problems that currently exist. These problems have been correctly identified by the RAG investigations.
3	<p>Do you agree with the proposed Code amendment which would introduce a new category of default when the following conditions are satisfied:</p> <ul style="list-style-type: none"> a. the retailer is no longer entitled to trade on a distribution network because its use of system agreement has been terminated due to a 'serious financial breach' by the retailer b. no unresolved disputes remain between the retailer and the distributor c. the retailer has not taken timely steps to arrange a customer switch d. the distributor has been unable to remedy the situation e. the distributor requests the Authority to initiate its process for managing an event of default. 	<p>Yes, we support the introduction of the new category. However, we would appreciate further explanation of the intent of point d (clause 14.45(h)(iii) of the draft amendment) before we could fully support these proposed conditions.</p> <p>Our reading of point d leads us to question the value of its inclusion, as we are unsure why the onus is being placed on the distributor to resolve the situation in a reasonable time when it would have been the retailer that triggered the termination of a use of system agreement because of a serious financial breach.</p> <p>If we have misinterpreted the meaning of this sub-clause we would argue that this supports the case for rewording it, as it is currently unclear. If we have interpreted it correctly we would appreciate further clarification from the Authority regarding the rationale supporting it and its intended application.</p>

4	Do you agree that the proposed Code amendment should apply not only to the network or networks across which the event of default has occurred? If not, why not?	Yes. We agree with the Authority's assessment that applying the process to only the network or networks across which the event of default has occurred could incentivise retailers to manipulate the market. Additionally, we note that Powerco's Use of System Agreements (UoSA) are agreed with retailers for our entire network. Creating the ability to terminate a UoSA for individual sub-networks would require multiple UoSAs with a single retailer. This would be a time consuming and costly exercise that would not add any value.
5	Do you agree that the trigger for the actions to be undertaken by the Authority should be limited to a breach of sub-clauses 14.55(a), 14.55(b), 14.55(f), and (the new) 14.55(h)? If not, why not?	Yes. Wherever possible, it is preferable for a retailer to trade out of trouble rather than trigger the default process, with the caveat that the retailer is able to continue to meet its financial obligations. We would also expect that, should the Authority be aware that a retailer was trading under any of the other sub-clauses (c, d, e and g) of clause 14.55, the retailer would be subject to close monitoring by the Authority. This should help ensure swift intervention by the Authority in the form of the proposed process if necessary.
6	Do you agree that the process for managing a retailer default should ensure that responsibility for all ICPs of the retailer in default, active and inactive, are transferred to another retailer? If not, why not?	<p>Yes. Ensuring that it is not possible to complete the default process with stranded ICPs is essential to the successful exiting of a retailer from the market. Any other outcome should be considered a failure to address all issues relating to retailer default.</p> <p>The Gas Industry Co has also recognised the unacceptable consequences of stranded ICPs occurring in its work on retailer default and is ensuring that this issue is fully addressed.</p>
7	Do you agree that the process should accommodate situations where the default might not be resolved but an acceptable resolution has been agreed and all payments that should have been made have been made? If not, why not?	Yes. By initiating the proposed retailer default arrangement when it is not a genuine case of a retailer breaching one of the trigger clauses, the Authority is in danger of negatively affecting the confidence of customers and industry participants.. As long as the Authority is notified and can observe the rectification of the error it should be acknowledged but nothing more.

8	Do you agree with the judgement arrived at by the RAG that a total period of 17 days for managing an event of default would provide a reasonable balance between the costs of too short a period and the costs of an extended period? If not, why not?	<p>Yes. We consider 17 days provides a fair balance for all parties involved and is based on solid economic analysis of the situation. Arguments will always be able to be made for shorter or longer periods based on industry participants' business drivers, but a line needs to be drawn and we consider the proposed amendments achieve that successfully.</p> <p>One point to note is that clause 14.55(h) of Part 14 details the termination of a retailer's UoSA due to a serious financial breach, as the trigger for the proposed process. As a distributor would have worked to remedy the situation and meet the termination requirements of a UoSA before terminating, there may be few possibilities to remedy the situation in the seven days provided.</p>
9	If a period of 17 days is maintained, should this time be allocated as follows: seven days for a retailer to resolve the dispute or transfer its customer base, seven days for customers to voluntarily switch to another retailer, and a maximum of three days for communication with customers and ensuring all switches are processed?	Yes. We consider these to be tight but achievable timeframes.
10	Do you agree that the Code should be amended to require a retailer in default to provide information on its customers to the Authority and for the Authority to obtain this information from distribution networks and the registry if the information is not forthcoming from the defaulting retailer? If not, why not?	Yes. As the total period for managing a default event is relatively short, quick and easy access to consumer information is essential if mandatory transfers are to be executed within the proposed timeline.

11	Do you agree that the Code should be amended to provide for the registry to complete the switch of any customer of a retailer in default that chooses to switch to another retailer, if the retailer in default does not meet its obligations under the switching rules? If not, why not?	Yes. Provisions need to be in place to ensure that the switching process can proceed successfully even if the defaulting retailer is not co-operating. If this ability did not exist it would undermine the whole process.
12	Do you agree that the Code should be amended to provide for the Authority to direct the registry not to complete the switch of any customer to a retailer in default after the Authority has advised the customers of that retailer that their retailer is in default and they should transfer to another retailer? If not, why not?	Yes. This is the simplest and most cost effective way of ensuring that no customers can switch to a retailer that has triggered the default process.
13	Do you agree that the Authority should advise retailers and other interested parties that an event of default has occurred, and if it considers appropriate, identify the entity in default, to enable these parties to make necessary preparations? If not, why not?	Yes. However, consideration should be given to how to manage the release of this information so as not to exacerbate the defaulting retailer's problems in the seven days it has to resolve the cause of the default.
14	Do you agree that the Code should provide for the Authority to communicate directly with the customers of the retailer in default, including via mass media? If not, why not?	Yes. Centralising communications by having the Authority assume this responsibility is the most effective and efficient mechanism for ensuring that customers receive consistent messages. Having the Authority co-ordinate communications brings a degree of impartiality that should help assure customers that the messages they are receiving are both correct and important.

15	Do you agree that the Code should provide for the Authority to provide customer information to the retailers to whom it transfers customers, should a mandatory transfer be required? If not, why not?	Yes. As the body playing the facilitation role in the mandatory transfer of customers, the Authority is the logical responsible party.
16	Do you agree that the Code should be amended to require that contracts between the retailer and its customers provide for the Authority to assign the contract to another retailer if an event of default is unresolved after 17 days? If not, why not?	Yes. Having provisions that allow for the mandatory transfer of customers is the only way to ensure that stranded ICPs do not occur. The mechanism to accomplish this can vary, but the principle of not having any stranded ICPs at the end of the default process is non-negotiable.
17	Do you agree that the terms offered by a recipient retailer (who is assigned customers by the Authority) should be those terms (including price) normally offered by the recipient retailer at the date the Authority was notified of the default? If not, why not?	Yes. We consider this to be a fair compromise for both retailers and customers. One concern we have regarding the terms offered by recipient retailers is that consumers should retain the option to switch retailers at any time after the transfer without penalty. If this were not to be the case, as indicated by the proposed clause 11.15A.1(c), which would require a customer to pay an amount for cancelling a contract before the expiry of a minimum term, we believe there would be a negative effect on consumer welfare and the efficient operation of the market.
18	Should the arrangements for managing an event of default provide for the Authority to tender the remaining customer base of the retailer in default after the Authority had exercised its rights to assign the contract on the terms of the recipient retailer? If not, why not?	No. We do not believe that allowing for a tender process would improve the overall arrangements for managing a default event. Consumers are going to understand the need to switch retailers from the Authority's communications, and those retailers that would benefit commercially from acquiring new customers will aggressively pursue those consumers. Consequently, at that point in the process, we believe the market should be left to operate without further intervention.

19	<p>If a tender arrangement is provided for, should the Authority invite tenders on the basis of the prices that would be charged to the customers by the recipient retailer (but no higher than standard terms offered by that retailer) with the Authority assigning the customers on the basis of the lowest priced retailer? If not, why not?</p>	<p>Yes. If a tender arrangement were introduced to the process, the proposed approach to tendering should help avoid problems relating to rights to monies received when a liquidator is involved.</p>
20	<p>Do you agree that, should the Authority be required to allocate customers of the retailer in default, it should do so on the basis of market share in the relevant networks but without any de minimus threshold? If not, why not?</p>	<p>Yes. Allocating by market share is a fair mechanism with high visibility. We also consider that the random allocation of ICPs to retailers is an important process step that should help ensure that no single retailer receives a higher number of ICPs that have a poor payment history due to, for example, the demographics of the localities of the ICPs concerned.</p> <p>As a principle we support the future proofing of the Code by not including detail in clauses that may vary in the short to medium term. For this reason, we agree that a de minimus threshold mechanism would not be the best solution.</p>
21	<p>Do you agree that the arrangements for managing a retailer default should provide an opportunity for any retailer that is assigned customers to object on the basis that the assignment would threaten its financial viability, with the onus on the retailer to substantiate such a claim? If not, why not?</p>	<p>Yes. It is highly likely that if a retailer finds itself in a position that triggers the default process, the whole market would be experiencing increased financial pressure, e.g. due to high wholesale prices. Consequently, a mechanism needs to be in place to ensure that assigning customers to a retailer will not force the retailer concerned into a difficult financial position. While the proposal to allow retailers to object could be an adequate mechanism, it should not be allowed to delay the overall process, which should still be able to be completed within 17 days. If this mechanism were approved we would expect the assessment of any objection to remain confidential between the Authority and retailer.</p>

22	Do you agree that the Code should require that the recipient retailer is responsible for notifying their assigned customers that they were now a customer of the recipient retailer, and advising the terms and conditions of their new contract? If not, why not?	Yes. The Authority's responsibilities should end when a customer is switched to a new retailer. From then on, it should be the new retailer's role to manage the relationship.
23	Do you agree that the Code should require that contracts between retailers and their customers should include provisions that: provide for the retailer to give customer details to the Authority in the event of a default; allow the contract to be assigned by the Authority in the event of default, with the terms and conditions to be replaced by the recipients retailer's terms and conditions; provide for the retailer to assign the contract? If not, why not?	Yes. Through the RAG consultations the industry has developed the most effective and balanced way to manage a retailer default situation. For this process to function properly, the provisions proposed would need to be required to be included in customer/retailer contracts.
24	Do you agree the proposed amendment is preferable to the other options? If you disagree, please explain your preferred option in terms consistent with the Authority's statutory objective in section 15 of the Electricity Industry Act? If not, why not?	Yes, we agree that the proposed amendment is preferable to the other options. While we consider the full retailer of last resort option has merits, we agree with the Authority's assessment of the benefits and limitations of that approach and believe that the proposed amendment is preferable. Two key attractions of the full retailer of last resort option are its simplicity and ability to fit within the tight time period. We consider that any proposed amendment should have these attributes and this is one of the reasons that we have reservations about introducing the competitive tender element into the process.

25	Do you agree that a period of 17 days strikes the right balance to achieve the benefits of an arrangement for managing an event of default while minimising the costs of achieving those benefits? If not, what period of time should be specified and why?	Yes. We recognise that it is a case of balancing the two sets of costs and we believe the 17 day period does this effectively. For distributors, the proposed 17 days is important as the prudential requirements mandated under Part 12a of the Code have increased distributors' potential exposure to bad debt in addition to the potential two months' financial loss they may already face before the proposed process starts.
26	Do you agree that the benefits of the proposed arrangements would exceed the costs? If not, why not?	Yes. Although the benefits of the proposed approach are difficult to quantify, they are almost certain to exceed the relatively small costs associated with implementing the changes.
27	Do you agree that the proposed arrangements meet the Authority's Statutory Objective? If not, why not?	Yes. The proposed arrangements are consistent with the Authority's statutory objective and not to make the changes would be inconsistent with the objective. A key element of the arrangements that we support is allowing time to develop a commercial solution to resolve an insolvency situation before regulatory intervention occurs. We also believe that the proposed approach minimises any possible negative effect on retail competition.
28	Do you have any comments on the drafting of the proposed amendment?	<p>We would like further clarification of the meaning and purpose of the following proposed amendments:</p> <p>Clause 11.15A.1(c) the terms of the assigned contract to be amended on such an assignment to include a minimum term in respect of which the customer must pay an amount for cancelling the contract before the expiry of the minimum term; and</p> <p>Clause 14.55(h)(iii) the distributor has not been able to remedy the situation in a reasonable time; and</p>