

More standardisation of UoSAs - consultation paper

Response to submissions

24 February 2015



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1 Introduction

- 1.1 The Electricity Authority (Authority) is examining a range of issues associated with the way that distributors and retailers develop and enter into use-of-system agreements (UoSAs).¹
- 1.2 The Authority published a consultation paper on 8 April 2014 which sought feedback on a proposal to achieve more standardisation of UoSAs. The Authority considered that adopting more standardised UoSAs would provide long-term benefits for consumers. It would do this by promoting competition in the retail market and by promoting more efficient operation of the electricity industry.
- 1.3 The consultation paper also sought feedback on matters arising from what the Authority had observed about how participants responded after the Authority published model UoSAs (MUoSAs) in September 2012. The consultation paper discussed a range of matters, including:
 - (a) the Authority's view of the observed behaviours relating to the uptake of the MUoSAs and expectations of more standardisation of UoSAs
 - (b) the consequences of these behaviours and the implications on achieving the competition and efficiency objectives of the MUoSAs
 - (c) a range of high-level response options the Authority is considering
 - (d) the Authority's preferred option (require reset of all existing interposed agreements and introduce a default agreement (with departure by agreement only) for distribution service into the Code), including preliminary views on the likely costs and benefits of that option.
- 1.4 The consultation paper and full copies of the submissions received are available on the Authority's website at: <http://www.ea.govt.nz/development/work-programme/retail/more-standardisation-of-use-of-system-agreements/consultation/#c12201>.
- 1.5 The Authority published a summary of submissions paper in November 2014, which can also be found on the website by following the link above.
- 1.6 At the same time, and also available on the same webpage, the Authority published its responses to a number of legal and process issues that were raised by some submitters.
- 1.7 The purpose of this paper is to provide the Authority's responses to the remaining topics included in submissions that were not addressed in the legal and process responses paper.

¹ Refer Electricity Authority, 2014/15 work programme, Table 1 (page 5), project 1.9. The work programme is available at, <http://www.ea.govt.nz/about-us/strategic-planning-and-reporting/our-work-programme/>.

2 This paper follows the same structure as the summary of submissions

- 2.1 The structure of this paper is the same as the structure of the summary of submissions paper.
- 2.2 Section 3 of the summary of submissions paper outlined that submitters' comments were grouped into five main areas, reflecting the structure of the consultation paper:
- (a) Section 4 of the paper summarised submissions on the Authority's approach to the more standardisation of UoSAs project, and focused on legal and process issues raised. As noted in paragraph 1.5, responses to these issues have been provided in a separate response paper and are therefore not repeated in this paper.
 - (b) Section 5 of the paper summarised submissions on questions 1 to 4 of the consultation paper, which were about the issues identified by the Authority and the problem definition. The Authority's responses to these matters are provided in section 3 of this paper.
 - (c) Section 6 of the paper summarised submissions on questions 5 to 13 of the consultation paper, which were about the merits of the options to achieve more standardisation that were set out in the consultation paper. The Authority's responses to these matters are provided in section 4 of this paper.
 - (d) Section 7 of the paper summarised submissions on questions 15 to 16 of the consultation paper, which were about the Authority's preliminary assessment of the benefits and costs associated with establishing default terms for UoSAs. The Authority's responses to these matters are provided in section 5 of this paper.
 - (e) Section 8 of the paper summarised submissions on question 17 of the consultation paper, which was about the Authority's initial assessment of MUoSA terms that might be suitable to be core terms in a default UoSA. The Authority's responses to these matters are provided in section 6 of this paper.
- 2.3 Section 7 of this paper summarises the Authority's high-level view after considering all submissions, and sets out the next steps the Authority intends to take.
- 2.4 Some of the questions in the consultation paper overlapped. Similarly, the summary of submissions paper noted that some submitters' responses overlapped or were for more than one question. Further, some submitters provided general comments that related to two or more questions. This paper

therefore provides responses to the common topics or themes raised in submissions.

3 The issues identified and the problem definition

- 3.1 Sections 2 and 3 of the consultation paper provided background relevant to the consultation paper. The Authority had suggested there may be competition and efficiency-related problems with the way that some participants were responding to the publication of MUoSAs in September 2012. These sections also set out the sequence of events and information gathering that led to the Authority reaching that conclusion.
- 3.2 Section 4 of the consultation paper discussed the Authority's policy objectives and expectations when it published MUoSAs in September 2012. It also discussed the consequences of the participant behaviours the Authority had observed through its information gathering throughout 2013 and early 2014.
- 3.3 The Authority requested feedback on these matters so it could develop an up-to-date picture of:
- (a) the issues in the consultation paper (question 1)
 - (b) the level of recent activity between distributors and retailers related to developing, negotiating and agreeing UoSAs (question 2)
 - (c) any relevant new issues (question 3)
 - (d) any new developments that would provide additional information or update the situation (question 4).
- 3.4 Thus, the focus of this part of the consultation paper was whether, and if so to what extent, there is a problem that warrants the Authority's attention.
- 3.5 Sections 2, 3 and 4 of the consultation paper prompted submissions across a range of views. In this section we first summarise the key submission themes from questions 1 – 4 and then provide a response at the end of the section.

Question 1 – the issues outlined in the consultation paper

- 3.6 This question asked: "Do you have feedback that would update the issues outlined in this section?"
- 3.7 Submitters had a range of views. These were summarised by submitter rather than by topic in paragraphs 5.6 – 5.34 of the summary of submissions paper. This paper does not repeat the summaries by submitter (which were quite lengthy and are published on the Authority website). Instead the paper distils key themes for each question and provides the Authority's responses to these themes. This approach is adopted throughout the response paper.

- 3.8 The key themes for question 1 relate to the extent to which the submitter supported the Authority's preliminary view that a problem existed or not. This prompted submissions on:
- (a) whether a problem existed that justified regulatory intervention
 - (b) the pace of distributor and retailer activity in negotiating new UoSAs since publication of the MUoSAs in September 2012
 - (c) views on the context surrounding Vector's negotiation of new UoSAs with retailers
 - (d) the fitness for purpose of the published MUoSAs.

Is there a problem?

- 3.9 In general, distributors submitted that a lack of standardisation of UoSAs between distributors is not a problem in terms of competition and/or efficiency effects. They also considered that the level of transaction costs of developing variations to UoSAs has been overstated and is likely to be outweighed by other benefits. Those benefits include maintaining flexibility to develop terms appropriate to unique circumstances and ensuring that contracts reflect actual commercial practice within the industry.
- 3.10 In contrast, many retailers and MEUG considered that a problem with the lack of UoSA standardisation does in fact exist, which impacts adversely on competition and efficiency. Submitters expressing this view considered that the process of negotiation with some distributors was frequently frustrating, time consuming and expensive. They also submitted that a 'take it or leave it' approach was commonly encountered. This was because distributors placed a high value on signing essentially the same agreement with all retailers trading on their networks. Consequently, the distributors were unwilling to vary terms at the request of an individual retailer.

The rate of progress

- 3.11 Distributors generally considered the rate of progress was satisfactory but noted that many distributors and retailers were unwilling to commit further resources to developing and negotiating UoSAs until the Authority's had concluded its review process.
- 3.12 A frequently expressed view was that the Authority's review had commenced very early in the 3 – 5 year period that the Authority had expected for updating legacy UoSAs.

Vector's process

- 3.13 Some submitters considered that the Authority's focus on Vector's UoSA development and negotiation process was inappropriate, or that the Authority had drawn incorrect conclusions, or both.

- 3.14 Some retailers noted that the goal of achieving a single unified approach covering distribution services across Vector's two legacy network areas was a one-off situation that required Vector and all retailers to enter into new UoSAs. In response, retailers generally took a pragmatic approach in accepting the terms and conditions Vector offered so as to achieve the benefits provided by Vector's newly unified approach. Some considered that the earlier versions of the Vector UoSA departed materially from the September 2012 MUoSA and were one-sided in Vector's favour. They noted, however, that later versions incrementally returned the drafting to something more closely aligned with the MUoSA.

The fitness for purpose of the September 2012 MUoSAs

- 3.15 Some submitters considered that some of Vector's modifications to the MUoSA provided superior terms.
- 3.16 One submitter expressed the view that the September 2012 MUoSA would not be fit for purpose as a regulated form of agreement without further development.

Question 2 – activity relating to development and negotiation of UoSAs

- 3.17 This question asked: "If you are a distributor, are you actively developing and negotiating UoSAs with retailers? If you are a retailer, are you actively engaged with any distributors in relation to UoSAs? Please provide information relating to your approach, experiences, successes and concerns."
- 3.18 Distributors generally considered that good progress had been made in moving to new UoSAs, mostly based on the published MUoSA. ENA surveyed its membership on the matter and reported on the status of some 24 of 29 local distributors. Some smaller distributors felt that some retailers did not want to commence negotiations with them until they had finalised arrangements with larger distributors.
- 3.19 In general, while some retailers considered that some good progress had been made, they expressed a range of frustrations. These collectively described an environment with significant ongoing uncertainty about:
- (a) whether and when counterparties would actively engage in UoSA negotiations
 - (b) what the starting point would be (ie, which pre-existing UoSA or MUoSA version would be used to develop new UoSAs)
 - (c) how much effort would be required in any negotiation
 - (d) how much unnecessary duplication and additional resource would be required in any new negotiation.

Question 3 – any new issues or concerns that may have arisen

Question 4 – any new developments that would provide additional information or update the situation presented in section 4 of the consultation paper

- 3.20 Question 3 asked: “Are you aware of any new issues that have arisen since the Authority undertook monitoring and communication with participants relating to UoSAs in early 2013?”
- 3.21 Question 4 asked: “Are you aware of any new developments that would provide additional information or update the situation presented in section 4? If so, please provide relevant details”.
- 3.22 These questions prompted some closely-related and overlapping submissions and are accordingly addressed together.
- 3.23 Submitters noted a range of corollary issues, including:
- (a) distributors continuing to offer materially misaligned UoSAs
 - (b) the uncertainty caused by the Authority’s review and the reluctance to commit further resource to UoSAs in the meantime
 - (c) a proliferation of embedded networks being created, frequently without UoSAs being offered by network owners, and another issue related to the Authority’s current approach of providing guidelines for drafting UoSAs suitable for embedded network use
 - (d) some other relatively minor matters.

Authority’s response to submissions on questions 1 - 4

- 3.24 Having considered all of the feedback on this topic, the Authority remains of the view that significantly enhanced standardisation of the terms and conditions in contracts for the supply of distribution services by 29 individual local distributors is a desirable goal in attaining the Authority’s statutory objective. At the same time, retaining the flexibility to develop mutually beneficial innovations in the way distribution services are provided is also a desirable goal.
- 3.25 The degree to which standardisation can be practically applied to the full range of terms that variously deal with core commercial matters on the one hand and operational matters on the other, is a matter to be further considered and developed.
- 3.26 The Authority concludes that a greater degree of regulatory certainty is a desirable goal in pursuit of its statutory objective. This will conclude more than a decade of development of (currently voluntary) model terms covering the supply of distribution services.
- 3.27 The Authority notes the frequently expressed view that its most recent review work and consultation on this topic has led to new regulatory uncertainty. The

Authority considers, however, that such uncertainty was inevitable given the practices adopted by some distributors and some retailers since the publication of MUoSAs in September 2012. Relying on voluntary participant behaviours has not resulted in a durable regime, as some participants have interpreted the Authority's objectives in different ways.

- 3.28 The Authority considers the best way to provide regulatory certainty is to develop a default UoSA which will be closely based on the existing MUoSA. Refinements to the MUoSA will likely be made during the development process in order to make it suitable as a default agreement and to incorporate drafting improvements in specific areas.
- 3.29 However, concurrent with this process, the Authority expects distributors and retailers to continue to negotiate UoSAs comparable to the key components of the existing MUoSA. As required by section 39(2)(b) of the Electricity Industry Act 2010, the Authority will undertake an evaluation of the costs and benefits of its Code amendment proposal. If parties do negotiate agreements similar to the MUoSA, then the benefits of establishing a default UoSA would unlikely be as high as they currently are. If the Authority considers the benefits of the proposal would not exceed the costs, then it would be unlikely to introduce a default UoSA.

4 The merits of the options identified in the consultation paper

- 4.1 Sections 5 and 6 of the consultation paper discussed the Authority's preliminary conclusions following its information-gathering work. The Authority concluded in that paper that less participant discretion in the way that distributors and retailers form UoSAs would likely be required. Sections 5 and 6 also outlined the range of options the Authority was considering to better achieve its statutory objective.
- 4.2 The Authority requested feedback on:
- (a) its view that its objectives for more standardised UoSAs are unlikely to be achieved by persevering with largely voluntary measures (question 5)
 - (b) any options that would be worth considering in addition to those identified in the consultation paper (question 6)
 - (c) the design detail provided in the Authority's description of the options (question 7)
 - (d) whether there are any issues relating to variations in network connections standards between distributors (question 8)
 - (e) whether the options intended to require distributors and retailers to transition to new UoSAs represent the range of options available to the Authority, and whether any other options should be considered (question 9)

- (f) the Authority's initial assessment that option 4 is the best approach to meet its objectives (question 10)
 - (g) what other Code design details should be considered if option 4 were subsequently adopted for development (question 11)
 - (h) whether there is a problem in the way that distributors that adopt the conveyance approach contract with retailers and consumers, and whether standardisation of conveyance UoSAs should be pursued as well (question 12)
 - (i) whether a problem exists in the way that embedded network owners contract with retailers, and whether standardisation of embedded network UoSAs should be treated the same as local networks (question 13).
- 4.3 Sections 5 and 6 of the consultation paper prompted submissions with a range of views.

Question 5 – is persevering with voluntary measures likely to achieve efficiency and competition objectives for UoSAs?

- 4.4 This question asked: "Do you agree that the Authority is unlikely to achieve its objectives for UoSAs within a reasonable timeframe by persevering with largely voluntary measures? Please state the reasons for your view".
- 4.5 Responses to the question were broadly divided. Distributors broadly expressed support for retention of the status quo (option 0), possibly augmented with clearer guidelines and expectations by the Authority (option 1).
- 4.6 Amongst the retailer submissions, Contact and Trustpower also supported keeping voluntary approaches. Contact considered that the Authority needed to clarify its expectations and encourage parties to voluntarily update their legacy agreements to reflect good industry practice. Trustpower considered that the Authority was interfering in commercial arrangements in a way that would introduce unnecessary transaction costs for all participants.
- 4.7 All other retailer submitters and MEUG took the opposite view, supporting the Authority's view that less voluntary measures would be necessary to provide significantly enhanced regulatory certainty and to achieve greater competition and efficiency benefits. Some submitters considered that improved drafting within UoSAs negotiated since publication of the MUoSAs should be included as part of developing less voluntary means to standardise UoSAs.

Authority's response

- 4.8 Having considered all submitted views on the question, the Authority considers that no persuasive case has been made that voluntary measures alone will achieve greater levels of standardisation for UoSAs and, in turn, promote competition and efficiency for the long-term benefit of consumers. While most submitters agreed that standardisation is a desirable goal underpinning the

statutory objective, opinions remain significantly divided as to how standardisation may be achieved while maintaining flexibility to innovate service terms and conditions at the margin.

- 4.9 Thus, the Authority remains of the view that less voluntary measures are necessary. They will provide regulatory certainty and standardise terms and conditions of service that tend to remain validly constant over time. They will be flexible enough to step out of the way when parties develop genuinely innovative changes. A process will be developed for incorporating such innovations in the MUoSA (and therefore in the default UoSA) over time.

Question 6 – other options to be considered

- 4.10 This question asked: “What other options can you suggest that would be worth considering alongside the options identified in section 5.2 and explained in more detail in section 5.3? Please explain the key advantages of your suggested option(s)”.

- 4.11 Submitters suggested a number of other options. For the most part, these described further detail within the options in the consultation paper. They included:

- (a) ensuring the MUoSA is updated to reflect recently negotiated clauses, including those developed by Vector
- (b) a process that brings together a representative working group of retailer and distributor commercial managers to see if they can reach agreement over recently negotiated clauses
- (c) forming a default agreement for a specific distributor where at least three of the five ‘major retailers’ have previously agreed to a specific form of agreement (else the MUoSA becomes the default)
- (d) a suggestion that all new UoSAs become public and that the Authority comments on any variations
- (e) requiring parties to seek Authority approval for any variations they seek to make from the MUoSA
- (f) including default standards for information exchange protocols for distributors and retailers to use.

Authority’s response

- 4.12 The Authority has noted all suggestions made by submitters and considers that some have merit for further development. The Authority agrees that the September 2012 MUoSA could benefit from an update in specific areas and, irrespective of the option ultimately adopted, agrees that the recent development and negotiation of UoSAs by participants is likely to have resulted in improved drafting. However, the Authority is not intending to make significant or wholesale

changes to the MUoSA, which was developed over the past decade with considerable input from stakeholders.

- 4.13 In respect of suggestions that participant representatives are brought together in a working group to agree detailed drafting, the Authority remains of the view that this is unnecessary and unlikely to achieve durable alignment or broad representation. Likewise, suggested arrangements in which a number of large, well-resourced incumbents effectively act to set the terms and conditions that apply to smaller entrants are unlikely to promote competition.
- 4.14 The Authority supports suggestions about the need for the contents of UoSAs to become more transparent. The Authority notes that the September 2012 MUoSAs included guidelines for a voluntary disclosure regime but that most distributors have not implemented this.
- 4.15 In respect of suggestions that the Authority approve amendments on an individual basis, the Authority considers it is not appropriate that it take on this role. A regular review process will be developed for incorporating improvements in the MUoSA over time.
- 4.16 Information exchange protocols are already available to participants in the form of the EIEPs published by the Authority and updated from time to time. Whether their use is voluntary or a regulated requirement is a standardisation matter separate from consideration of the UoSAs.

Question 7 – feedback on design detail

- 4.17 This question asked: “What feedback do you have on the design detail discussed in this section? What options amongst the design detail do you think would best meet the Authority’s objective?”.
- 4.18 Responses to this question provided a number of suggestions for developing the detail of a default UoSA regime.

Authority’s response

- 4.19 The most common theme noted from submissions was that further work is required to update the current MUoSA into a form suitable for whichever option is adopted.
- 4.20 The Authority acknowledges that many submitters have provided their views on this question (or have elected not to) at an early stage of this review, at a point where the Authority’s preferred option was not yet established. Accordingly, the Authority has noted all suggestions in respect of detailed design and agrees that further consultation around the detail of the preferred option will be necessary. However, the Authority is not intending to make significant or wholesale changes to the MUoSA, which was developed over the past decade with considerable input from stakeholders.

Question 8 – potential issues relating to network connection standards

- 4.21 This question asked: “Are you aware of any issues relating to the variation of network connection standards between distributors that the Authority should consider? Are there opportunities to provide greater standardisation of network connection standards? Why would network connection standards not be suitable for greater standardisation across distribution network areas?”.

Authority’s response

- 4.22 Responses to this question indicate there may be a valid question in respect of the lack of standardisation of network connection standards between distributors. However, the Authority is persuaded that this is a separate question to improving how UoSAs are put in place in accordance with the Authority’s statutory objective. The Authority agrees that further consideration is out of scope for this project and should be held over to a separate review.

Question 9 – options for requiring distributors and retailers to transition to new UoSAs

- 4.23 This question asked: “Do you agree that the extended options described in section 6.4 reasonably represent the range of options available to the Authority in seeking to meet its objectives for more standardised, efficient and pro-competitive UoSAs? If you disagree, please describe what other options should be considered and what advantages these options would provide?”. Section 6.4 sets out 7 options identified by the Authority.
- 4.24 Submissions broadly supported the range of options for transition proposed in the question. Some submitters argued that UoSAs agreed since September 2012 should not be interfered with in any regulated transition away from legacy UoSAs.

Authority’s response

- 4.25 Having considered submissions, the Authority remains of the view that a reasonably prompt transition from legacy UoSAs to new UoSAs based on significantly more standardised terms and conditions is closely aligned with the Authority’s statutory objective, particularly in respect of the competition and efficiency limbs.
- 4.26 Consideration of further detail for a suitable mechanism will be considered in the next stage of the project.

Question 10 – is option 4 the best approach?

- 4.27 This question asked: “Do you agree with the Authority’s initial assessment that option 4 (require reset of all existing interposed agreements and introduce a default agreement for distribution service into the Code) is the best approach to meet its objectives?”.

- 4.28 This is a key question in the context of the Authority's review of the processes surrounding the development and negotiation of UoSAs between distributors and retailers.
- 4.29 It is evident after considering all submissions that there is no clear consensus on the best way to move forward. However, some reasonably common themes have emerged.
- 4.30 As noted earlier, in general, distributors and some retailers (Contact and Trustpower) favour one of the status quo options. Some of those expressing this view are further of the view that if the Authority were to progress a less voluntary option, one of the default options would be the next best alternative.
- 4.31 Also as noted earlier, the remaining retailers and MEUG are of the view that one of the less voluntary options (ie, options 3 – 6) is essential if certainty and standardisation are to be achieved.
- 4.32 A further commonly expressed view is that distributors' operational practices vary considerably (albeit selected from amongst a quite small number of options that broadly represent good industry practice) and should not be standardised at this time (or, at least, should be considered on a case by case basis as separate exercises outside of considering standardisation of UoSAs).

Authority's response

- 4.33 The response provided to questions 1 – 4 provides background to the Authority's response to question 10. In response to questions 1 – 4, the Authority concluded that a problem does in fact exist. Question 10 explores the likely best option for resolving the problem.
- 4.34 Section 5.2 of the consultation paper provided a diagram (Figure 1) that depicted the spectrum of options available. At one end, the more status quo-like options (ie, the low numbered options) emphasised maximising flexibility and discretion for distributors and retailers. This would allow them to develop, negotiate and execute UoSAs that best meet their needs as essential service providers in the service chain that provides delivered electricity to consumers. Experience over many years has shown that this end of the spectrum of options has resulted in:
- (a) a low level of standardisation of terms and conditions across retailers trading on a network
 - (b) a low level of standardisation of terms and conditions for a single retailer trading on multiple networks
 - (c) inefficient outcomes
 - (d) lower levels of competition than might otherwise occur.
- 4.35 In the early 2000s, shortly after network and retail functions were separated, participants recognised it was desirable to standardise terms and conditions of distribution services, emphasising:

- (a) efficiency, for the benefit of both distributors and retailers
 - (b) competition, in the interests of entrant and expanding retailers.
- 4.36 Thus, the model UoSA initiative was commenced with generally broad participant interest and support. Input from a wide range of stakeholders was received throughout the subsequent ten-year process.
- 4.37 However, support for standardisation initiatives has not been universal, since:
- (a) some participants are relatively large, experienced and/or well-resourced and can usually obtain the terms and conditions of service they prefer
 - (b) several large incumbent retailers have been operating across all networks since the early days of retail competition. As a result, they have already incurred the costs of negotiating UoSAs for all networks and gained the experience needed to trade on all networks. Ongoing inefficiencies through a lack of standardisation are seen to some degree as a low priority issue that applies to all competing retailers
 - (c) some (early incumbent) retailers have *possibly* obtained favourable terms and conditions compared with their competitors by selling their legacy network businesses (although the status quo arrangements provide no transparency over legacy UoSAs that would conclusively prove this assertion).
- 4.38 The other end of the spectrum of options (ie, the higher numbered options) emphasised maximising standardisation and limiting discretion for distributors and retailers to vary from standardised approaches. While a small number of submitters have expressed support for introducing mandatory terms and conditions, such an approach would be very difficult to develop and could have unintended adverse consequences.
- 4.39 Between these extremes are two options that seek to balance the desirable attributes of standardisation and flexibility. Under these options (options 3 and 4 in the consultation paper), a regulated benchmark or default agreement of 'core terms' would be published. The core terms would apply when either or both parties to a UoSA preferred it over the alternative of agreeing an alternative agreement.
- 4.40 Parties would have flexibility to negotiate away from the core terms, allowing them to deal with unforeseen events and innovative new approaches. It would also be possible to universally update all current agreements based on the default, if that would better meet the Authority's statutory objective and follow due process.
- 4.41 There are precedents for such an approach already in place applying to connection of distributed generation (in Part 6 of the Code) and transmission agreements (in Part 12 of the Code).

- 4.42 In respect of agreeing so-called ‘operational terms’, there are effectively three primary options. Option 3 in the consultation paper left the negotiation of operational terms to the counterparties. Under that option, the Authority would expect distributors to seek to standardise such terms to reflect the operational practices they currently adopt.
- 4.43 Option 4 contrasted with this approach by proposing a default set of operational terms. Some submitters appear to have assumed option 4 would require that a single set of operational terms for all networks in New Zealand. Others seem to have assumed that a set of operational terms *relevant to each distributor’s current operational practices* would be developed and published.
- 4.44 When developing the consultation paper and option 4 in particular, the Authority had simply not gone into this degree of detail. The Authority considers it currently impractical and inappropriate to propose absolute standardisation across all distributor operational practices. That said, it is likely that cases for standardisation of particular operational practices will be considered as separate reviews in the future, as has occurred from time to time in the past.
- 4.45 So to clarify, option 4 (default whole agreement) would regulate:
- (a) a set of default core terms introduced into the Code that would apply if either party to a UoSA negotiation preferred this over the alternative of negotiating and agreeing alternative core terms
 - (b) a process to establish a single set of default operational terms *for each distributor* that, together with the default core terms in (a), would comprise a default whole agreement.
- 4.46 If both parties agree to negotiate away from the default, they would be free to do so. In this way, option 4 retains the possibility of outcomes consistent with the status quo option (option 0) *but only where both parties agree*. This provides choice but corrects the imbalance of negotiating power frequently encountered between distributors and retailers.
- 4.47 In summary, the Authority considers that option 4, as clarified in the preceding paragraph, would best balance the desirable attributes of flexibility and standardisation and provide regulatory certainty. It would thus best meet the Authority’s statutory objective, particularly the competition and efficiency limbs.

Question 11 – design details for option 4

- 4.48 This question asked: “What other Code design details should be considered if option 4 were subsequently adopted for development?”.
- 4.49 Submitters made a range of suggestions related to:
- (a) the status of legacy UoSAs
 - (b) participant engagement and transition

- (c) the transparency of terms within UoSAs.

Authority's response

- 4.50 Paragraph 6.5.10 of the consultation paper listed a number of key design details relating to the default and mandated group of options (ie, options 3 – 6). Each of these areas will receive further detailed consideration at the next stage of the review but at this stage the Authority provides the following responses.

The status of legacy UoSAs, engagement and transition

- 4.51 An 'existing UoSA' is any current agreement that applies to a distributor and a retailer covering the provision of distribution services to the retailer. Current UoSAs are most commonly agreements. Some early agreements are understood to have been amended over time in accordance with the variation provisions of the original agreements. In some cases, side letters are understood to have been used to record amendments. It is also possible that agreement of some matters is not formally recorded in writing but is simply given effect by mutual assent and practice.
- 4.52 Some existing UoSAs are up to approximately 15 years old while others have been very recently executed. The consultation paper highlighted the Authority's desire to update legacy UoSAs, particularly those that were negotiated within a quite different regulatory environment (ie, around the time of the sale and purchase of distribution and retail businesses, circa the year 2000).
- 4.53 The Authority has noted the frequently expressed comments about the status of the more recently concluded UoSAs, particularly where these have been based on a recent MUoSA and both parties remain comfortable with the outcome.
- 4.54 Owing to the wide variety of starting positions, a pragmatic approach is required. Having considered submitted views, the Authority considers the following approach is workable with respect to engagement and transition:
- (a) The Authority would determine a date (the 'commencement date') as the commencement date for the proposed new arrangements applying to UoSAs.
 - (b) At any date before the commencement date, either party may trigger adoption of the default whole agreement relevant to the distributor in question. This right applies equally to the distributor, all currently trading retailers and potential new entrant retailers in the course of their introductory engagement with the distributor.
- 4.55 If both parties to an existing UoSA are happy to remain bound by that agreement, the agreement can remain in place and become an 'alternative agreement' as at the commencement date. This option would likely be limited to UoSAs executed after 1 October 2012. The Authority considers this approach could in theory allow some legacy agreements to remain in place. However, the process would trigger

a review of such agreements in all cases and require some action on the part of the counterparties to review them. It is expected that on review, either party would be sufficiently concerned with one or more of the legacy provisions such as to trigger a fresh negotiation and possible adoption of the default agreement.

Transparency of the terms within UoSAs

- 4.56 Support for greater transparency was not a theme taken up in many submissions, though some support was expressed in response to question 11 and earlier questions. As well, there were no submissions supporting less or no transparency.
- 4.57 The Authority considers that transparency of the terms and conditions of distribution service agreements is a cornerstone of a robust and durable regulatory regime. The agreements underpin the objectives of providing all retailers with equal access to distribution services and even-handed treatment by distributors.
- 4.58 The Authority currently considers that none of the matters relating to the even-handed provision of distribution services could reasonably be considered to be commercially sensitive or confidential to the counterparties. The Authority will consider any case made in support of commercial sensitivity and confidentiality in subsequent stages of the project.

Question 12 – conveyance arrangements

- 4.59 This question asked: “What information do you have that a problem exists in the way that distributors that adopt the conveyance approach to establish contracts with retailers and consumers? Should standardisation of conveyance UoSAs be pursued as well?”
- 4.60 From the submissions received on this question, the situation relating to conveyance agreements is clearly a lower priority for participants compared with interposed agreements. This likely reflects the fact that conveyance arrangements are adopted by only two distributors. However, there was some support for the objective of consistency of treatment in the formation of agreements between distributors and retailers.

Authority’s response

- 4.61 The Authority notes the arguments made in favour of including conveyance agreements in the current review but does not intend to consider them further at this stage because:
- (a) under conveyance arrangements, distribution services are contracted directly with each end consumer – thus, the nature of the services provided between distributors and retailers is different compared with interposed arrangements

- (b) the competition and efficiency drivers are much diminished compared with interposed arrangements since conveyance arrangements are adopted by just two of the smaller distributors
 - (c) a conveyance MUoSA is already in place and an option 0 or 1 approach would seem to be appropriate, at least in the short term while resources are focused on higher priority areas
 - (d) the Authority doubts that what might be perceived a more liberal treatment of conveyance arrangements would be a decisive factor in a distributor's consideration of a change from interposed to conveyance arrangements.
- 4.62 Accordingly, the Authority has opted to defer considering conveyance agreements further at this stage. In choosing this course, the Authority reminds participants that it remains open to feedback on an ongoing basis related to new problems that might arise related to conveyance arrangements and practices.

Question 13 – embedded networks

- 4.63 This question asked: “What information do you have that a problem exists in the way that embedded network owners establish contracts with retailers? Should standardisation of embedded network UoSAs be treated the same as local networks?”.
- 4.64 Submitted views were divided as to whether a problem exists in the formation of UoSAs on embedded networks and whether further consideration should be progressed by the Authority within the current project that is currently considering local networks only.

Authority's response

- 4.65 The Authority's Retail Advisory Group is currently undertaking a review of secondary networks, which includes considering competition and efficiency issues with embedded networks. The Authority expects the RAG to report its recommendations during 2015. Subject to the RAG's findings, the Authority will consider the potential for more standardisation of embedded network UoSAs as part of its response to the RAG recommendations report.
- 4.66 Embedded network owners and retailers are reminded that this outcome provides an opportunity for relevant participants to demonstrate that voluntary approaches can work. Through the course of the papers published during the MUoSA development project, the Authority considers its expectations in respect of standardisation of UoSAs have been well communicated.

5 Preliminary assessment of benefits and costs of default terms

- 5.1 Section 7 of the consultation paper set out the Authority's preliminary assessment of the benefits and costs associated with moving to default terms for UoSAs.
- 5.2 The Authority asked for feedback on the assessment of costs and benefits, and particularly submitters' views on:
- (a) the average time and cost for a retailer and a distributor to negotiate and administer a UoSA on a local distribution network that the retailer is entering for the first time (question 14)
 - (b) the likely cost of adopting the default terms approach (question 15)
 - (c) the number of retailers likely to enter regions with less than 10 retail brands, with and without a default terms arrangement in place (question 16).

Question 14 – time and cost for entrant retailers negotiating UoSAs

- 5.3 This question asked: "Based on your experience negotiating UoSAs, what is the average time and cost for a retailer and a distributor to negotiate and thereafter administer a UoSA on a local distribution network that the retailer is entering for the first time?".

Question 15 – likely cost of adopting the default terms approach

- 5.4 This question asked: "Based on your experience adopting the UoSA clauses contained in Part 12A of the Code, what do you estimate the cost to be of adopting the default terms approach?".
- 5.5 Some submitters considered that the Part 12A experience was not particularly relevant to the question posed.

Question 16 – number of retailers likely to enter into regions

- 5.6 This question asked: "Based on your experience with electricity retail competition, and with reference to Figure 2, over the next two to five years on average what number of retailers (being retailers likely to enter into UoSAs) would you expect to see entering regions with less than 10 retail brands, under the following two scenarios: a) *without* a default terms arrangement in place, and b) *with* a default terms arrangement in place?".

Authority's response to questions 14 – 16

- 5.7 The Authority notes the range of feedback provided in response to these three questions and will consider this in more detail at the appropriate point in the review.

6 Assessment of core terms

- 6.1 Appendix B of the consultation paper provided a clause by clause assessment of whether the interposed MUoSA terms would be suitable as core terms, if the Authority were to proceed with a default or mandatory approach.
- 6.2 The Authority requested feedback from interested parties on its initial assessment (question 17).

Question 17 – UoSA core terms

- 6.3 This question asked: “The column headed “Suitable for inclusion in core terms?” in Appendix B provides the Authority’s initial view of the parts of the interposed MUoSA that would be suitable for direct transfer into a default or mandatory agreement, if such an approach were adopted. Do you agree with the assessments provided here for each clause and schedule? Please reference your responses to specific clauses and schedules and provide reasons if you disagree”.
- 6.4 Submitters provided a range of views on the detail included in Appendix B, including one view that including Appendix B in the consultation paper implied that the Authority had already made a decision on the outcomes of its review.
- 6.5 Some submitters made the point that further detailed consideration would be required if a default UoSA is eventually put in place.

Authority’s response

- 6.6 The Authority appreciates the feedback provided in response to question 17 and will further consider the detail in subsequent stages of the review.
- 6.7 In including Appendix B in the consultation paper, the Authority did not intend to imply that it had already made a decision. Indeed, the consultation paper points out that no decision had at that point been made and that submissions would be taken into consideration before making a decision. The detail in Appendix B (and other sections) was necessary to enable informed feedback on how the various options under consideration would work.

7 Summary and next steps

Summary of the Authority’s current views

- 7.1 The Authority appreciates the significant efforts by submitters in developing submissions on the consultation paper and acknowledges the range of sometimes strongly opposed views on how best to proceed. This is an important piece of the regulatory framework in the context of the Authority’s statutory objective, particularly in respect of the competition and efficiency limbs.

- 7.2 The Authority's responses to submissions made on each of the questions should have provided an indication of the Authority's updated views and intended next steps. However, these responses are somewhat fragmented and focused on separate areas, so the next section summarises the Authority's high level view and its intended process from here.

Headline view – does a problem exist?

- 7.3 Having considered all submissions received on the consultation paper, the Authority remains of the view that significantly enhanced standardisation of the terms and conditions related to supply of distribution services by 29 individual local distributors is a desirable goal. At the same time, retaining the flexibility to develop mutually beneficial innovations in the way distribution services are provided is also a desirable goal.
- 7.4 The degree to which standardisation can be practically applied to the full range of terms that variously deal with core commercial matters on the one hand and operational matters on the other hand, will be further considered in the next stage of the project.
- 7.5 The Authority has further concluded that a greater degree of regulatory certainty than currently exists is a desirable goal, so as to bring to a durable conclusion more than a decade of development of (currently voluntary) model terms covering the supply of distribution services. For a variety of reasons, reliance on voluntary participant behaviours has not resulted in a durable regime.

Headline view – what is the best option to resolve the problem?

- 7.6 In section 5 of the consultation paper, the Authority proposed a spectrum of options that described progressively greater prescription in the way a UoSA's terms and conditions could be established.
- 7.7 At one end, options based on retention of the status quo would emphasise flexibility for parties to bilaterally negotiate and execute UoSAs.
- 7.8 At the other end, options proposing mandatory terms and conditions would emphasise standardisation of terms and conditions across and within networks.
- 7.9 The consultation paper presented the Authority's preliminary view that the best balance between complete flexibility and absolute standardisation appeared to be an option based on introducing a default agreement that would act like a benchmark agreement. Under this approach, either party could prefer the default over any alternative agreement but the parties would remain free to mutually agree to alternative terms (which could be as simple as varying a single term from the default). This approach is consistent with the approach taken in connection of distributed generation (under Part 6 of the Code) and in establishing transmission agreements (under Part 12 of the Code).

- 7.10 Having concluded its consideration of submitters' feedback, the Authority remains of the view that introduction of a default agreement based largely on the existing MUoSA would address the problem described in the consultation paper in accordance with its statutory objective.
- 7.11 To summarise, option 4 (default whole agreement) would regulate:
- (a) a single set of default core terms introduced into the Code that would apply if either party to a UoSA negotiation preferred this over the alternative of negotiating and agreeing alternative core terms
 - (b) a process to establish a single set of default operational terms *for each distributor* that, together with the default core terms in (a), would comprise a default whole agreement.
- 7.12 If *both* parties agree to negotiate away from the default they are free to do so at any time. In this way, option 4 retains the possibility of outcomes consistent with the status quo option (option 0) *but only where both parties agree*. This provides choice but corrects the imbalance of negotiating power frequently encountered between distributors and retailers, and will therefore improve retail competition.

Participants should continue to negotiate UoSAs

- 7.13 To provide regulatory certainty and to avoid stifling participants' progress in negotiating UoSAs, the Authority intends to develop a default UoSA which will be closely based on the existing MUoSA. Refinements to the MUoSA will likely be made during the development process in order to make it suitable as a default agreement and to incorporate drafting improvements in specific areas. However, the Authority is not intending to make significant or wholesale changes to the MUoSA, which was developed over the past decade with considerable input from stakeholders.
- 7.14 The Authority expects distributors and retailers to continue to negotiate UoSAs comparable to the key components of the existing MUoSA. As required by section 39(2)(b) of the Electricity Industry Act 2010, the Authority will undertake an evaluation of the costs and benefits of its Code amendment proposal. If parties do negotiate agreements similar to the MUoSA, then the benefits of establishing a default UoSA would unlikely be as high as they currently are. If the Authority considers the benefits of the proposal would not exceed the costs, then it would be unlikely to introduce a default UoSA.

Next steps

- 7.15 The Authority intends to develop a further consultation paper that addresses the following:
- (a) more detailed design of option 4, what it would contain in respect of the rights and obligations of the counterparties, what processes would be necessary and how it would be introduced into the Code

- (b) a draft set of core terms for a default agreement developed from the September 2012 interposed MUoSA and incorporating more recently developed experience from negotiations
- (c) a draft of a detailed process for establishing default operational terms on a distributor by distributor basis
- (d) a commencement and transition process.