Submissions

Electricity Authority

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15th October 2019

To whom it may concern,

**ENA submission to Electricity Authority *Code amendment proposal: Default Distributor Agreement* consultation**

The Electricity Networks Association (ENA) appreciates the opportunity to make a submission to the Electricity Authority (the Authority) consultation on “Code amendment proposal: Default Distributor Agreement”.

ENA represents the 27 electricity distribution businesses (EDBs) in New Zealand (see Appendix A) who own and operate the local electricity lines that are critical to the well-being of communities throughout the country. ENA’s submission is on behalf of our members and in addition to any individual submissions that they may make.

ENA accepts that the Authority may introduce a Default Distributor Agreement to govern the relationship between traders and distributors with respect to the provision of distribution services. However, we have many concerns with the proposed drafting of the Default Distributor Agreement and associated Code amendments (hereafter referred to collectively as the DDA) contained in the consultation material. We urge the Authority to consider our comments, and those of our members, carefully, as it may be very difficult to address errors or omissions once the DDA comes into effect.

Because of the significance of the Authority’s proposals, we strongly encourage the Authority to run a two-stage consultation process and allow cross-submissions from interested parties following this first stage. This will help to ensure that any inadvertent errors or oversights in the DDA drafting can be identified and amended prior to the proposals coming into effect in the Code.

We have limited our comments and proposed amendments to the most important issues that we consider are essential to achieving the Authority’s objectives and ensuring that the DDA functions efficiently and in the interests of all market participants. We have grouped our comments and amendments under the following themes:

* **Contract formation, variation and termination** – No contract is designed to last forever. Circumstances and the parties’ requirements will change over time. In an unregulated environment, parties manage these risks through specified contractual terms and provisions relating to amendment, termination and renewal. In a regulated environment, where parties are required to offer to contract on regulated terms, it is important to consider how these risks will be managed. As currently drafted, Part 12A contemplates evergreen contracts with limited options for updating and revision. This creates unacceptable risks to all market participants and means there will be inevitable variance between the practical commercial realities on the ground and the distribution agreements that are in force. We have therefore proposed a number of targeted safeguards to ensure that distribution agreements can evolve appropriately, within the overall structure of a regulated must-offer standard contract.
* **Risk management** – In the proposed drafting of the DDA, the Authority has presumed to determine the appropriate balance of risk and liability between EDBs and traders. This is a significant intervention for the Authority to make and should be undertaken with the utmost care and caution. As a general rule, risk should be allocated to the party best able to bear it. The Authority has failed to set this balance correctly in the current DDA drafting. The consequence is that the costs associated with these risks will be borne by consumers through regulated distribution prices. We have therefore made targeted comments relating particularly to prudential and indemnity arrangements to ensure an appropriate allocation of risk.
* **Access to data** – ENA is pleased to see that the Authority has taken a pro-active approach to enable EDBs to access metering consumption data via traders in the drafting of Appendix C of Schedule 12A.1. Unfortunately, there are several proposed restrictions on the use of consumption data that will significantly undermine its usefulness to EDBs, and therefore potential benefit to consumers. There are also improvements that could be made to this drafting that would ease some of the administrative and logistical burden on both EDBs and traders whilst still providing appropriate safeguards for the management of this data. We have proposed amendments to resolve these issues.
* **Workability** – there are a number of areas in which the current drafting is insufficiently clear, appears to give rise to unintended consequences, or does not account for some of the practical realities of the environment in which distributors operate. We have therefore suggested a number of changes to improve the workability of the DDA. In our view, these should be uncontroversial.

We expand on each of these themes in the body of our submission. A detailed explanation of our proposed amendments and the reasons for them is set out in Annex A to this submission. We also enclose mark-ups of Part 12A and the draft DDA showing our proposed amendments (in track changes).

**Contract formation, variation and termination**

As currently drafted, when a trader elects to contract under them, the DDA will apply in perpetuity. There is no mechanism by which the EDB can elect to amend, update or terminate the agreement without the trader also agreeing to do so (other than a mechanism to amend operational terms). This locks distributors into an evergreen contractual arrangement that can never evolve to reflect changes in market conditions or the parties’ reasonable requirements.

Over time, this inflexibility could become increasingly onerous for the EDB as they are unable to keep the terms of the various DDA contracts synchronised to their internal businesses process (which will naturally change over time) and one another.

In addition, it is difficult to foresee or predict with any certainty how the electricity market in New Zealand might develop over time. The current roles and responsibilities, both of industry participants and regulators, could quite conceivably change significantly in a comparatively short space of time. In the face of such uncertainty, the contracts between EDBs and traders formed under the DDA would continue to operate provided the traders in question wished them to do so.

This level of inflexibility is also unnecessary to achieve the Authority’s objectives. Consistency and stability can still be achieved alongside reasonable mechanisms to ensure that the process of entering into, and operating under, the default distribution agreement, does not create unnecessary risks to EDBs or to market functioning.

Our key changes in relation to these issues include:

* providing greater flexibility to enter into alternative agreements at a later date, and in relation to the subject matter of the Appendices;
* establishing a mechanism to periodically refresh all distribution agreements to reflect the distributor’s current DDA;
* allowing distributors to apply to the Authority for an exemption from the requirement to offer the DDA to address the risk of rogue traders;
* specifying the circumstances in which the Rulings Panel may unilaterally amend operational terms;
* obliging the Authority to periodically review Part 12A of the Code and the template DDA to ensure it remains fit for purpose; and
* removing from the DDA the obligation to comply with guidelines promulgated by the Authority from time to time. It is inappropriate for the Authority to arrogate to itself a parallel rule-making power that bypasses the statutory framework for amending the Code through the Electricity Industry Act.

We provide further detail below in relation to certain of these proposals.

*Power to exempt distributors from the obligation to contract with rogue traders*

The DDA gives traders the absolute right in all circumstances to trade on an EDB network with no scope for the EDB to refuse them. This has the effect of transferring some risk from traders (particularly new entrant start-up retailers) to the EDB, and via the EDB charges to other consumers.

Over the last 12-18 months EDBs have seen a marked increase in the number of traders defaulting on their payments for distribution services. This then triggers a relatively lengthy process for the EDB to remove the trader in question from their network, often incurring bad debts which are borne by both retailers’ and EDBs’ wider consumer base.

Under the DDA proposal, there would be no mechanism by which an EDB could stop a trader that has defaulted in the manner above from simply establishing a new DDA with the EDB and starting again.

We note that this balance of risk that has been struck by the Authority for the relationship between traders and EDBs is significantly different to the risk the wholesale electricity market (via the clearing manager) carries for these traders.

We do not think the Authority has set the balance of risk between traders and EDBs (and by extension their consumers) appropriately. If the Authority is of the view that the benefits of competition brought about by supporting traders in this way is in the public interest, then the additional risk borne by EDBs should also be carried to a similar extent by the wider electricity industry, via the wholesale market clearing manager.

We propose that distributors be permitted to apply to the Authority for an exemption from the requirement to contract with traders that persistently fail to comply with their obligations. It would be within the Authority’s discretion whether or not to grant that exemption.

*Rulings Panel’s discretion to amend operational terms*

ENA has significant concerns that the role of the Rulings Panel, the scope of its determinations, and the effects that these might have upon agreements made under the DDA, are insufficiently defined in the current draft Part 12A. As currently drafted, the principles for operational terms are not clearly articulated and it is not clear that the Rulings Panel is required to identify an actual error before it intervenes to substitute its own terms.

It is also not clear to us how determinations made by the Rulings Panel would flow through into agreements made between the EDB in question and other traders , if at all. If these do flow through, would the other traders, who might be quite content with their existing agreement with the EDB, be happy? If they do not flow through, would the EDB end up having to support multiple different sets of operational terms for different traders? Either outcome could be unsatisfactory for the parties involved.

We have proposed narrow and targeted amendments to:

* clarify the principles for operational terms;
* make clear that the Rulings Panel, before it exercises its power to amend, must be satisfied that the operational term in question is actually inconsistent with the principles, as opposed to intervening merely because it has identified an alternative term that it considers is also consistent, or more consistent, with the principles; and
* require the Rulings Panel to consider the impact on the distributor of adopting the amended term.

*Inappropriate rule-making through guidelines*

ENA believes that it is inappropriate of the Authority to include within the DDA an absolute requirement for EDBs to comply with several guidelines issued by the Authority. This requirement has the effect of elevating what were simply guidance documents to the status of quasi-regulation, something that they were never intended to be. It also bypasses the statutory framework for rule-making through the Code. These documents were not subject to the rigorous development processes that true regulations would be subject to and are also not subject to the same level of consultation and scrutiny should they be revised in the future.

Finally, it creates unacceptable risk to all market participants, because it means that key obligations in distributor agreements are open to redetermination on an ad hoc basis through revisions to the guidelines. This represents a significant and avoidable inefficiency.

**Risk management**

We consider that the Authority’s proposed prudential security regime is largely ineffective because:

* the cost of posting additional security is prohibitive, and allows traders to earn a risk-free return significantly in excess of cost of capital; and
* the amount of security an EDB can require of a trader is insufficient to reflect the true extent of the risk posed by the trader defaulting.

There are also a number of issues with the structure of the liability and indemnity provisions that will lead to unintended consequences and unnecessary cost and risk for distributors. These costs will ultimately be borne by consumers through regulated prices, and therefore should be minimised to the extent possible. We have proposed targeted amendments to improve the functioning of the risk allocation mechanisms of Part 12A and the DDA.

**Data access**

ENA applauds the changes that the Authority has made to the DDA to allow EDBs to access smart meter consumption data via traders. We note that this is entirely consistent with the recommendations arising from the Government’s Electricity Price Review, and the recently published Government response to those recommendations.

Whilst the principle is sound however, there are several requirements in the proposed Appendix C that are overly onerous, to the point of rendering the consumption data provided to EDBs useless. These are as follows:

* **Inability to combine data:** as drafted the proposed Appendix C prohibits EDBs from combining data with any other date without the consent of the trader. Without such consent, the data is essentially worthless, as it cannot be combined with any pre-existing network information to generate a benefit to the EDB (and ultimately EDB consumers). The ‘permitted purposes’ defined in Appendix C should be sufficient to ensure that the data is used for appropriate reasons, and therefore this requirement for trader consent prior to combining data sets should be removed.
* **Overly onerous audit requirements:** Appendix C currently allows for each individual trader on an EDB network, where they are providing smart meter consumption data to that EDB, to undertake an audit of the EDBs data handling processes. In the extreme, this could lead to as many as 38 trader audits per annum, which is clearly inefficient and unnecessary. EDBs are already subject to multiple different audit regimes and, if this audit is genuinely required, it would be better to include it within one of the pre-existing audits on behalf of all traders. For example, the Authority’s participant audit process may be an appropriate place for this to sit.
* **Requirement to destroy data after use:** similar to the point made above, the requirement to destroy smart meter consumption data after use will, at best, significantly reduce the benefit that EDBs can generate from that data. At worst, it will render the data worthless and completely remove any benefit that might otherwise have been obtained. In practice, many of the benefits that EDBs can generate from the use of smart meter data will be informing certain decisions on network planning and these decisions will need to be justified after the fact. Also, the ability to monitor and track consumption over time to inform decision-making will be another key benefit arising from use of the smart meter data. In both these scenarios these benefits will be unobtainable, or significantly inhibited, by the requirement to destroy data.

We have also made a number of proposed changes to address ambiguities or potential inaccuracies in the current drafting.

**Workability**

Asides from the major issues described above, there are a range of issues that go to the workability of the agreement that we wish to bring to the Authority’s attention. These are detailed in the Annex and should be uncontroversial. We highlight the most significant issues below:

**Load Control:** the DDA should allow for future development of load control. The availability of consumer load to other parties (EDBs, traders, others) should be at that consumer’s discretion. The DDA as drafted does not allow for consumers to benefit from future opportunities that might arise related to load control. Specifically,

* clause 5.1 is just based on a price category selection – this is how it has been done in the past. New TOU price plans, the removal of Low Fixed Plans, multiple traders, new technology (e.g. controllable EV chargers) may mean that it is not a simple price category selection. We have made a change to clause 5.1 to permit consumers, at their discretion, to take advantage of other load control options offered by distributors.

**Conveyance contracts:** similar to the point above, these consumers are obtaining distribution services (small “d” small “s”), but not via a Direct Customer Agreement (as defined in the DDA) as they are billed for network services via their retailer. The contract is backward looking with the assumption that the retailer provides energy. In the future, the customers may be their own supplier of the energy and EDBs should have scope to provide layers of distribution services. Our key points include the following:

* Traders can use an EDB network to provide their energy to consumers who are being billed for conveyance services by the EDB (current key accounts) and that EDBs are responsible for the debt.
* EDBs should be able to offer distribution services (or a subset of distribution services) to consumers directly.
* Perhaps the simple approach is to remove the words “at the Customer’s written request” and rather have “as agreed by the Customer or Customer’s agent”. And adding some wider wording and removing the “unless otherwise agreed with the Trader, includes the direct billing...” in the definition sections.

**Billing:** EDBs need to be able to issue pro forma invoices, not just actuals to reflect current practice. The best approach may be to have the issuing of invoices section (9.3) inserted as an operational term at the back of the contract. This would allow EDBs to improve billing processes to allow new pricing options to be implemented and promote greater retail competition and consumer benefits. For example, EDBs may be able to help some small new entrant retailers billing consumers weekly by aligning their billing with the new entrant retailer’s billing process, etc.

* Alternatively, the definition of Tax Invoice could be amended to make sure it can include EDB pro forma invoices.
* Or perhaps, by amending clause 9.2, EDBs could issue an estimated tax invoice even if the information is provided on time.

If you would like to discuss any of the points raised in this submission in further detail please contact Richard Le Gros (details below).

Yours sincerely,

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Electricity Networks Association

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**Appendix A – ENA Member Companies**

Alpine Energy

Aurora Energy

Buller Electricity

Centralines

Counties Power

Eastland Network

Electra

EA Networks

Horizon Networks

Mainpower NZ

Marlborough Lines

Nelson Electricity

Network Tasman

Network Waitaki

Northpower

Orion New Zealand

Powerco

PowerNet

Scanpower

The Lines Company

Top Energy

Unison Networks

Vector

Waipa Networks

WEL Networks

Wellington Electricity

Westpower