25 September 2012

Retail Advisory Group
c/- Electricity Authority
PO Box 10041
Wellington 6143

by email: rag@ea.govt.nz

SUBMISSION ON RETAILER DEFAULT SITUATIONS

1 Orion New Zealand Limited (**Orion**) welcomes the opportunity to comment on the second "Retail customers in retailer default situations" discussion paper (the **paper**) released by the Retail Advisory Group (**RAG**) in August 2012.

2 In general, we support the RAG's preferred approach. However, as we stated in our submission on 19 March 2012 on this matter, we believe the Authority has exacerbated the possibility of disconnection in the event of retailer default with its recent changes to prudential requirements. The arrangements proposed in the RAG's preferred approach, while sensible, are the ambulance at the bottom of the cliff. We believe that the Authorities first priority must be a restoration of appropriate prudential requirements to ensure appropriate time is allowed manage customers in the event of a retailer defaulting.

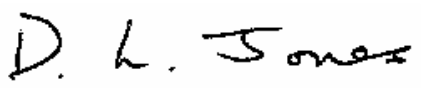
3 We consider that it is in customer's interests that they can have a reasonable expectation that a retailer they choose can meet its obligations. Confidence Knowing that the regulatory regime has good standards and retailers are required to meet appropriate prudential requirements is a key pre-requisite

4 Our submission is in the form of a response to a number of the paper's specific questions as an appendix.

Concluding remarks

5 Thank you for the opportunity to make this submission. Orion does not consider that any part of this submission is confidential. If you have any questions please contact Dennis Jones (Industry Developments Manager), DDI 03 363 9526, email dennis.jones@oriongroup.co.nz.

Yours sincerely



Dennis Jones
Industry Developments Manager

Appendix: Responses to specific questions

Question	Response
Q1. Do you agree with the summary of the options available to a distributor in the event of a default by a retailer, or are there other remedies available to a distributor?	We do not consider that the paper clearly articulates the options available to a distributor in the event of a default by the retailer. One of the options available to distributors is to disconnect customers, however we agree with the paper that it would be untenable for a distributor to disconnect en-mass customers because the retailer had not paid its bill. It is for this reason that distributors (and others) where strongly opposed to the recent Code changes reducing the level of prudential security that a distributor could require. As we noted in our early submission of 19 March 2012 "*we believe that the Authority has exacerbated the possibility of disconnect in the event of a retailer default with its recent changes to the prudential requirements".* A first priority must be putting the fence at the top of the cliff by restoring adequate prudential requirements this should help avoid the use of the ambulance at the bottom to transfer customers to another retailer. We question whether it is actually as straightforward as the paper appears to suggest for distributors to insist on only offering an conveyance agreement. We would expect explicit regulation would be required.
Q2. Do you consider that a distributor could be	We do not believe that we would change our contracting model as a result of our

sufficiently concerned about the prospect of a default by a retailer to insist on a conveyance use-of-system agreement for the use by retailers of its network, and if so, would this be an undesirable outcome?	concerns in relation to retailer default. However, we believe that there have been a number of Code changes and issues such as: • *Reduced prudential requirements* • *Indemnification of retailers under section 12A* • *Additional registry requirements* • *The introduction of MEPs* • *Standardised pricing formats* • *Retailer default* that of themselves may not cause a distributor to be sufficiently concerned about their contracting arrangements but when taken together do raise questions. Whether this would be an undesirable outcome possibly goes to the heart of the industry reforms that created the current regime. If all distributors moved to interposed agreement and billed their customers directly the role of retailers has to be questioned. However, an option could emerge where distributor bill the energy component for the retailer as a service, (effectively the completion at the generation level) this may prove to be more efficient than the status quo. Whether or not distributors moving to only a interposed agreement (whether billed directly or via the retailer) would result in a desirable or undesirable outcome requires far more consideration and consultation than is possible under this paper. However, Orion has been offering and operating both conveyance and interposed arrangements from the beginning of this regulatory regime. The interposed arrangements we provided are to meet customer requests for a direct contracting arrangement with Orion and may be either in the form of an arrangement where we directly bill the customer

	or our services may be billed via a retailer.
Q3. Should a distributor, after terminating a use-of-system agreement with a retailer as a result of an unresolved serious financial breach by that retailer, have an option of advising the Authority that it considers an event of default exists and that this event should be subject to the proposed arrangements under the Code to manage an event of default?	Yes, we believe that this is a positive improvement. It will also allow the Authority to be aware any pending default issues eg a retailer that may be under financial stress from defaulting on a distributor while continuing to pay the clearing manager to avoid regulatory intervention. We also consider that besides introducing this step the Authority should also revoke the recent change to the Code to limit the prudential requirements that distributors may require from distributors.
Q4. Are there any other events not currently captured by clause 14.55 that should be defined as an event of default and if so on what rationale?	No.
Q5. Should the Code provisions governing the notification of a default be broadened to require all participants and service providers to notify the Authority as soon as that entity has reasonable grounds to believe that an event of default is likely to occur, or has occurred?	Yes. We expect that this could allow earlier intervention by the Authority that may alleviate a default occurring. In the case that a default has occurred then the Authority should be made aware of this at the earliest opportunity.
Q6. Should the clearing manager have an obligation to advise an entity if it has not complied with a requirement of Part 14 of the Code and that this non-compliance is an event of default?	Yes, it may be an error that can be easily resolved if dealt with promptly.

Q7. Should the Code be clarified and simplified by bringing the actions that may be taken by the clearing manager in the event of a default into one sub-part and re-drafted to stipulate, to the extent practical, the actions the clearing manager would take in relation to a shortfall in payment or a failure to meet a call?	Yes. Clarification and simplification that assist participants in understanding the Code requirements and the actions that will occur should a default occur would be beneficial.
Q8. Should the Code stipulate that on being notified of an event of default, the Authority would immediately investigate and determine: a. whether an event of default exists; and b. if an event does exist whether that event is a minimal risk event arising from a technical or administrative failure that has or will be corrected within one business day or a commercial disagreement that doesn't affect the retailer's long-term ability to trade?	a) Yes. Immediate investigation and assessment should minimise participants exposure and consequential actions could limit financial loss. b) Yes. Even if the default is a technical or administrative failure, these events need to be documented • to ensure there are not delays while the Authority determines "root cause"; • to provide transparenty and check for any similar instances that might indicate more significant issues on the credit front; • to use as educational informationto assist other participants to reduce the risk of similar events.
Q9. Should any assessment by the Authority of whether the event is a minimal risk include a materiality threshold, equivalent to the serious financial breach threshold under the draft model use-of-system agreement?	Minimal risk should be covered by prudential requirements. Therefore anything exceeding the level of prudential requirements must be considered material.
Q10. If distributors are provided with an option of	a) No. The authority should not be tasked with assessing whether the distributor had

notifying the Authority that they had terminated a retailer's use-of-system agreement as a result of an unresolved serious financial breach, should the Authority be tasked with assessing whether the distributor had complied with the notice terms of the use-of-system agreement and, in the absence of action by the Authority, would be entitled to notify consumers that they would be disconnected unless they switched to an alternative retailer?	complied with the notice terms of the use-of-system agreement. That is a decision and process to be followed by the distributor and part of commercial arrangements. b) Yes, if the Authority did not act then distributor should be able to notify consumers that they would be disconnected.
Q11. Should the Code stipulate that on determining that an event of default of more than minimal risk exists the Authority would advise the retailer and its agent(s) that unless the default is rectified within a specified number of days, the Authority would: a. communicate with all of the retailer's customers advising them that their retailer had defaulted and that the customer should switch to another retailer and that if they did not switch by a specified date the Authority would assign them to another retailer; and b. proceed to terminate the retailer's rights to trade electricity under the Code?	a) Yes. However in practice we consider it will be very difficult for the Authority to communicate with all of the retailer's customers advising them that their retailer had defaulted and that the customer should switch to another retailer and that if they did not switch by a specified date the Authority would assign them to another retailer. We are interested in understanding how the Authority will do this in practice and in a reasonable time frame. b) We agree that the Authority should proceed to terminate the retailer's rights to trade electricity under the Code.
Q12. Should the Code require that retailers include an assignment clause in their customer contracts?	Yes. We agree in principle, however we foresee practical difficulties if the retailers receiving the customers are able to determine the prices and other terms on which they

	would supply the customers transferred to them.
Q13. What period of time, measured in days, is necessary to allow sufficient time for a retailer to transfer responsibility for its customers to another retailer or to rectify the default?	Without knowledge of the process we would suggest as quickly as possible and no more than 8 working days.
Q14. Should the relevant period of time be specified in working days or in calendar days?	Working days
Q15. Should a mechanism exist to extend the number of days provided to the retailer in default to rectify the event of default, including any interest payable, if that extension of time is approved by the parties who would bear the financial risk of an extended time period?	Yes, provided that at least the thresholds described in question 16 below are also put in place.
Q16. Should any extension of time for rectifying the default require approval of a majority in number representing 75% in value of the money owed or some other threshold?	Yes, this seems a reasonable compromise that has precedence in section 288 of the Companies Act
Q17. Should the Code provisions that provide for generators to be assigned or subrogated to the rights of the clearing manager be removed from Part 14?	No Comment

Q18. If, at the end of the eight-day period, the defaulting retailer has not satisfied the Authority that it (the retailer) is no longer in default, or has not transferred all of its customers to another retailer, should the Authority have the ability to communicate with the retailer's customers advising those customers that their retailer had defaulted, that they should switch to another retailer and, that if they did not switch by a specified date, the Authority would arrange for them to be transferred to another retailer?	Yes
Q19. Should the Authority be able to facilitate this voluntary transfer by providing the customer list of the retailer in default to competing retailers so that they may make their own approaches to the customers of the retailer in default?	We agree in principle, providing that competition issues are addressed.
Q20. What period of time, measured in days, should be provided by the Authority to the customer of the retailer in default to voluntarily switch to an alternative retailer?	It should be as quickly as practical and no longer than the 10 days provided for in the MUoSA.
Q21. Should the Code impose on retailers an obligation to have the following provisions in their contracts: a. in a default situation, the Authority may	Yes. Clarity for all parties as to the contractual arrangements in place is important.

terminate the contract between the retailer and its customer; and b. if the Authority terminates the contract under (a), the customer would become bound by a contract with another retailer stipulated by the Authority?	
Q22. Should retailers in the same network area be required by the Code to enter into contracts with customers of the defaulting retailer whose contracts have been terminated by the Authority?	It may be a step too far to oblige retailers in the same network area by the Code to enter into contracts with customers of the defaulting retailer whose contracts have been terminated by the Authority. This may escalate the problem and drive other retailers to default. There needs to be a mechanism to address the issue that a retailer taking on additional customers may not be in a financial position to take on additional customers without themselves risking default.
Q23. Should the Code provide for the Authority to invite other retailers to tender to provide contracts to the customers of the failed retailer whose contracts the Authority has terminated?	Yes
Q24. Should the Code enable the Authority to allocate, as a last resort, any remaining customers of the retailer in default amongst retailers on the affected network on a pro rata basis based on a historic retail volume measure?	In principle we agree, and all customers must be reassigned however as we noted in our response to question 22 this may escalate the problem and drive other retailers to default. It is not clear from the proposal how this issue will be addressed.
Q25. If you do not agree with a pro rata basis, what	No comment

method should the Authority use to allocate any remaining customers of the retailer in default amongst retailers on the affected network?	
Q26. Should responsibility for the customer, caused to be transferred by Authority, change to the new retailer on the date of the switch?	Yes, this would align with normal practice.
Q27. Should the Code be amended to require a retailer in default to provide the Authority with the information it would need to write to all of the retailer's customers advising them that the retailer is in default, and if necessary, to cause any remaining customers to transfer to another retailer?	Yes however it is important that customers are informed that information supplied by them may be used for this purpose.
Q28. Do you agree that to address the potential for information difficulties the Code should provide for the Authority to: a. advertise to advise customers of the retailer in default that they should choose an alternative retailer; b. access information held by the Registry and distribution utilities to reconstruct a customer database if necessary; and c. instruct the Registry to act as counterparty for customers switching voluntarily from the	Yes.

retailer in default, if required?	