Prepared for the Electricity Networks Association

Response to consultation paper: Default agreement for distribution services

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sapere research group

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1. Introduction

Nives Matosin and Toby Stevenson from Sapere Research Group were engaged by the Electricity Network Association (ENA) to prepare a comparison of the Authority's draft default distribution agreement (DDA) with the Model Use of System Agreement and the negotiated contracts of three distributors – Unison, Vector and WEL Networks (WEL) against the Electricity Authority's Statutory Objective.

Accordingly this report presents our independent assessment of the DDA and the comparators.

2. Our method

2.1 Analytical method and approach

The methodology compared the draft default distribution agreement (draft DDA) to the negotiated distributor agreements for Unison, Vector and WEL.

Our approach was to:

1. Use the DDA as the base case agreement to compare the negotiated agreements to.
2. Compare the DDA to the Model Use of System Agreement (MUoSA) for the changes and in particular any material changes and where clauses have been shifted to or from the Schedules or the Electricity Industry Participation Code (the Code).
3. Compare the clauses in the DDA to clauses in each of the three negotiated agreements. We also considered the impact of the DDA where clauses that were in the MUoSA have been omitted from the DDA.
4. Assess the DDA clause relative to the negotiated clauses against the impact on competition, reliability and efficiency (CRE) using the Electricity Authority's guidelines as the test.
5. Our assessment considers:
   (a) Where the clauses in the DDA and the negotiated agreements are the same there is no need to assess against CRE.
   (b) Where the DDA clause and the negotiated agreement differ, assess the variation against the CRE test. Where the DDA satisfies the CRE test better than the negotiated clauses then we recommend that the DDA clause stands.
   (c) Where a negotiated clause better satisfies the CRE test then we recommend that the negotiated clause should replace the DDA clause.
   (d) Whether some of the clauses would be to shift from the default core terms to the operational terms.
5. Assess how our recommendations are in the long term interests of consumers.

In some cases, there may be merit in moving clauses to the Code and we have noted where this may be the case.

2.1.1 Electricity Authority's statutory objectives

The Authority interprets its statutory objective as requiring it to exercise its functions in section 16 of the Act in ways that, for the long-term benefit of electricity consumers:

- facilitate or encourage increased competition in the markets for electricity and electricity-related services, taking into account long-term opportunities and incentives for efficient entry, exit, investment and innovation in those markets;

- encourage industry participants to efficiently develop and operate the electricity system to manage security and reliability in ways that minimise total costs whilst being robust to adverse events; and
- increase the efficiency of the electricity industry, taking into account the transaction costs of market arrangements and the administration and compliance costs of regulation, and taking into account Commerce Act implications for the non-competitive parts of the electricity industry, particularly in regard to preserving efficient incentives for investment and innovation.

We have been guided by the Electricity Authority's interpretation in our assessment.

2.1.2 Summary of key points from the Electricity Authority consultation paper

The Electricity Authority has stated that UoSAs influence the consumer experience in two ways:[1]

> • *Agreeing UoSAs: The more difficult or costly it is for a retailer and distributor to negotiate and agree a UoSA, the more it costs for those parties to do business. Those costs are reflected in the costs passed on to a consumer by the consumer's retailer. The costs of agreeing a UoSA may also discourage a retailer from trading on a network. Consumers are affected if there is less retailer choice on a network.*
>
> • *The terms and conditions of a UoSA: There are two aspects to this point. First, if a distributor does not treat retailers wanting to trade on the distributor's network even-handedly, by offering equivalent terms to retailers in similar circumstances, the retailers that have less favourable terms will potentially be put at a competitive disadvantage. Second, if a distributor imposes inefficient terms on all retailers on its network, that could restrict competition and innovation.*

In the first dot point, the Authority is expressing concern about transaction costs. In particular, that the cost of agreeing an agreement may discourage retailers to trade and thus reduce consumer choice (i.e. competition). This concern relates to technical efficiency, that the cost of doing business may be so high as to discourage retailers from competing in the first place.

In the second dot point, the Authority is suggesting the possibility that offering unequal terms to different retailers may result in competitive disadvantage to some retailers. Secondly, it is suggesting that inefficient terms could restrict competition and innovation.

Our analysis is focused on assessing whether in our view, the clauses in draft DDA that differ from the negotiated agreements are better at meeting the statutory objectives.

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1 Electricity Authority 2016, Default agreement for distribution services, Consultation Paper, 26 January 2016, p. A.

3. Key findings

A key finding of our analysis was that none of the negotiated agreements was detrimental to the statutory objective. The differences in the negotiated agreements and the draft DDA and MUoSA primarily reflected operational practice and management of risk for each of the businesses. All the variances from the MUoSA and draft DDA were terms that had been negotiated with traders.

The current arrangement of negotiated agreements has allowed for innovation in the contractual arrangements between distributors and retailers in the cases examined.

In most cases, the clauses in the negotiated agreements that varied from the draft DDA were preferable in that they better met the Electricity Authority's statutory objective.

We have summarised our findings into general comments and then into each of the three limbs of the statutory objective – competition, reliability and efficiency with a final conclusion about the long term interests of consumers.

3.1 General comments

3.1.1 Good Electricity Industry Practice and liability

Currently the general obligations section in the draft DDA (clause 2.1) states that the purpose of the clause is intended to provide an overview of each party's obligations under this agreement and does not impose any legal obligations on either party. In the comparable clauses in both Unison and Vector negotiated contracts (clauses 2.1 and 2.2), the services and obligations of the trader and distributor are framed with reference to Good Electricity Industry Practice. The obligations are symmetrical, applying to both the trader and distributor. Greater certainty in the obligations of traders and distributors is a benefit to consumers.

The reference to Good Electricity Industry Practice in the listing of services and obligations provides a comprehensive cover for all the services and obligations in the agreement. Good Electricity Industry Practice is a well-known and defined term that provides a reference and boundary for standards and operations. This helps to provide a framework for determining liability in the industry. The term Good Electricity Industry Practice is referred to certain clauses in the draft DDA but a more comprehensive and certain approach would be to refer to it in the general obligation section at the start of the DDA. The benefits of greater certainty by referencing Good Electricity Industry Practice accrue to the trader and distributor. The draft DDA is intended to be a default agreement but in effect becomes a mandated agreement in the sense that it is compulsory for such an agreement to be available for adoption if an alternative agreement cannot be negotiated. As such it appears that the term 'will' that was used in the voluntary MUoSA is replaced by the term 'must'. The use of the term 'must' indicates that an obligation is imposed on a party (rather than a voluntary agreement). Overall this creates stronger obligations on parties to comply with the DDA where it is taken up.

The stronger obligation may have repercussions on liability of parties. While this is a legal question and beyond the scope of this analysis it may have repercussions on liability and insurance costs.

3.1.2 Evolution of agreements

The DDA includes several provisions adopted from Vector's Use of System Agreement (VUoSA). This is evidence that the voluntary regime has led to improvements. This includes:

- Clause 21.1(c) relating to Force Majeure Events has been amended to remove text that is unnecessary because of the reference to Good Electricity Industry Practice. This is based on clause 21 of the VUoSA.
- Clause 24 includes a new sub-clause 24.4, which clarifies that except as provided in clauses 24 and 25, the parties' liability to each other is excluded to the fullest extent permitted by law. This is based on clause 24.4 of the VUoSA.
- The draft DDA new clause 26 which sets out the procedural requirements that apply to the Distributor and Trader if a Customer makes a claim against the Trader in relation to which the Trader wishes to be indemnified by the Distributor. The drafting of clause 26 is largely based on the drafting of clauses 26.11 and 26.12 of the VUoSA.
- The Authority considers that it is appropriate to include a clause in relation to the conduct of claims setting out the parties' obligations if a third party makes a claim under clause 27. This clause is based on clause 26.17 of the VUoSA.

This type of development and evolution of agreements may be lost under a mandated DDA approach. This in itself stifles dynamic efficiency in the market.

3.1.3 Terminology

In clause 7.1 of the draft DDA reference to "Pricing Policy and Methodology" is changed to "Pricing Methodology". Clause 12A.19 of the draft code refers to "pricing structures". There is no reference to "Pricing Methodology" in Part 12A of the draft Code.

Therefore the definition of Pricing Methodology is unclear. Further, in clause 7.4 of the draft DDA, the term "Pricing Structure" is replaced with "Pricing Methodology" but the term is not defined. The term "pricing structures" implies setting the fixed and variable components of prices. Pricing methodology is a broader term, referring to cost allocation methods etc. Therefore the term "pricing methodology" needs to be clearly defined by the Electricity Authority. This also has implications for consultation costs as discussed in section 3.4.7.

3.2 Competition

3.2.1 Conveyance

Draft DDA clause 3.1 states that a Distributor may enter into a Direct Customer Agreement with a Customer at the Customer's written request, provided that any existing Customer Agreement between the Trader and the Customer is not a fixed term agreement. (emphasis added).

The draft DDA clause 3.1 currently appears to preclude distributors from entering into a conveyance contract where there is a fixed term agreement.This is a blunt barrier to distributors and customers entering into an agreement. It is a barrier to "competition" preventing the customer from entering into an agreement with the Distributor because of the proscription on distributors.This arrangement hinders customer choice and is not in the interest of consumers.

An alternative approach is set out in Vector's negotiated contract:

> *clause 3.1* ***Distributor may enter into Distributor's Agreement with a Consumer****: The Distributor may enter into a Distributor's Agreement directly with a Consumer at the Consumer's written request. The Distributor acknowledges that its entry into a Distributor's Agreement with a Consumer does not override any obligations of the Consumer to the Retailer during the term of any fixed term Electricity Supply Agreement.*

This clause is preferable to the draft DDA clause because it does not proscribe customer choice and complements the Trader's agreement.

3.2.2 Valid Direct Customer Agreement

Draft DDA clause 3.3 states that *the Trader must not knowingly supply electricity on a Conveyance Only basis to an ICP unless there is a valid Direct Customer Agreement in force in relation to the ICP.*

This clause seems to indicate that the obligation to supply on a conveyance only basis does not apply if the trader did not know the status of the ICP. The concern is that it places fewer onuses on the trader to check the status of the ICP.

Currently in the Registry, there is a field that records if the distributor has a conveyance contract with the customer. Therefore it is a straightforward process for a trader to check a customer's status.

As such, a preferable approach to the draft DDA would be to place a positive obligation on the trader to ensure that they have an obligation to know the contractual status of the ICP.

This provides greater certainty to the customer and the distributor that the contractual arrangements will be met.

3.2.3 Distributor may control load

Clause 5.1 of the draft DDA states that *if the Distributor provides a Price Category or Price Option that provides for a non-continuous level of service by allowing the Distributor to control part or all of the Customer's load (a "Controlled Load Option"), and the Customer elects to take up the Trader's corresponding price option that incorporates the Controlled Load Option, the Distributor may control the relevant part of the Customer's load in accordance with […]. (emphasis added)*

This clause seems based on a presumption that the trader will have a corresponding price option. If a trader does not have a corresponding price then it seems that the distributor would not be able to offer this service to customers. This hinders competition and customer choice.

In addition to the requirement in clause 5.1 of the draft DDA, Vector's agreement includes clause *6.1(b) the Distributor provides any other service in respect of part of or all of the Consumer's load*

advised by the Distributor to the Retailer from time to time (an "Other Load Control Option") with respect to the Consumer (who elects to take up the Other Load Control Option).

This clause allows for other types of load control services to be included in the agreement. This provides for greater customer choice and enhances competition for load control services.

It would be beneficial to include this type of clause into the draft DDA to enhance competition and also efficiency. (Refer also to section 3.4.4).

3.2.4 Limitations if Distributor elects to control the Retailer's load

In relation to situations when the Distributor elects to control the Retailer's controllable load (see the related draft DDA clause 5.6) Vector's agreement contains the provision that limits the Distributor's control only to the extent and for the duration necessary to fulfil its performance obligations as an asset owner in respect of managing System Security or managing the security of the Network (VUoSA clause 6.7).

This provision provides greater certainty to the Trader that the Distributor will not control the trader's load for any longer than necessary. This enhances competition and benefits the trader and the affected customer.

3.2.5 Process to change Pricing Methodology

The EA's drafting note for Clause 7.4 states that the clause "has been amended to include a requirement that the Distributor consult with the Trader if the Distributor intends to change its Pricing Methodology. That requirement was previously included in clause 12A.7 of the Code, but is now appropriately included in each distributor's DDA".

Notwithstanding the uncertainty about the definition of pricing methodology discussed in section 3.1 above, the requirements for such a consultation process may sit better in the Code.

Changes to the Pricing Methodology would be of interest to all traders and a wider group of stakeholders including customers and alternative energy providers. Therefore it may be more appropriate for the consultation procedures to be in the Code rather than the DDA which is an agreement between a distributor and trader(s).

3.2.6 Interference with the network

Draft DDA clause 12.7 Interference with the Network requires the Trader to ensure the customer does not inject or attempt to inject any energy in to the Network unless the Customer is also a Distributed Generator and there is a Connection Contract between the distributor and the Distributed Generator.

This requirement is important to maintain the integrity of the network.

However, if the definition of DG precludes specific technologies then this provision could hinder competition and innovation.

Also, limiting this clause to Distributed Generation could create a gap in protecting the network.

It would be preferable to draft this clause to be technology neutral. That is, a trader should be required to ensure any energy injection from a customer onto a network is subject to a Connection Contract between the customer and the distributor. This would be a benefit to network reliability as well as competition and innovation in the industry.

3.2.7 Notification of events of default

The draft DDA (clause 18.4) contains provisions that sets out requirements that in the Event of Default, that is a Serious Financial Breach (in case of trader); a material breach of the Defaulting Party's obligations that is not being remedied; and the Defaulting Party has failed on at least two previous occasions within the last 12 months to meet an obligation, then the other party may issue a notice of termination in accordance with clause 18.1 and, if the breach is a Serious Financial Breach by the Trader, the Distributor may notify the Electricity Authority and/or the clearing manager that clause 14.41(h) of the Code applies.

Instead of seeking termination following a breach, Vector's agreement provides for an additional step before seeking termination. VUoSA clause 20.4 includes:

> *(e) if the Retailer is the Defaulting Party, the Distributor may:*
>
> *(i) undertake a Temporary Disconnection of some or all of the ICPs supplied by the Retailer, in which case the Retailer will take all steps necessary to allow those disconnections to be made and will provide the information required by the Distributor in relation to such ICPs; and/or*
>
> *(ii) prohibit the Retailer from using the Network to supply any Point of Connection which is not currently supplied by it; and/or*

And

> *(e)(iii) […] the Distributor shall ensure that its notification to the Electricity Authority and/or the clearing manager is not inaccurate or misleading; and/or*
>
> *(f) exercise any other legal rights available to it.*

Vector's agreement contains similar provisions for Insolvency Event (regarding draft DDA clause 18.6) contains similar provisions for disconnection of ICPs before seeking a notice of termination.

This provision allows the trader seek to remedy the Event of Default rather than terminating the business. It gives the trader another chance. This is beneficial for competition.

3.2.8 Termination of agreement

Clause 19 of the draft DDA has deleted the provision allowing either party to terminate the Agreement by giving at least 120 days' notice. Instead, clause 19.1 provides that the parties may terminate the Agreement by mutual agreement.

This amended provision would prevent a distributor from having the ability to terminate the agreement with the trader and convert the supply arrangement to a conveyance model, without agreement from the trader. This would hinder a distributor from changing its business model. It's not clear what the benefit of the amendment is – nor what the Electricity Authority sought to achieve from this change.

Clause 19.2 of the draft DDA Termination of Agreement for Event of Default or Insolvency Event sets out termination provisions if a party has breached the Agreement and the breach is an Event of Default, or a party has become subject to an Insolvency Event.

Each of the negotiated agreements contains a type of 'last chance' provision stating that:

> *Such notice for termination will lapse if the defaulting party remedies the Event of Default or Insolvency Event (as applicable) prior to the notice of termination becoming effective or the other party withdraws or extends the effective date of its notice. (See Vector contract contains provision 21.2(b)).*

This provision seeks to extend the opportunity for the trader to remedy the situation before the distributor takes action. It demonstrates willingness to preserve the trader as long as possible. This is supportive of traders, especially fledgling ones and enhances competition.

Clause 19.5 (Trader remains liable for charges for remaining Customers) of the draft DDA sets out provisions which state that the trader *remains liable to pay any charges for Distribution Services that arise in relation to connected Customers that have not been switched to another trader, or whose ICPs have not been disconnected by the Distributor.*

Vector's agreement is consistent but adds the sentence *Within 5 Working Days of this agreement being terminated, the Retailer must notify the Distributor of all ICPs that have not been disconnected or switched to another retailer.*

This provides the distributor with greater certainty about the status of the ICPs and what the Trader may be liable for.

The WEL contract is consistent and includes the sentence:

> *The Retailer will procure in its Consumers Contracts the right to terminate supply of electricity by the Retailer through the Network to the Consumer upon termination of this agreement.*

This clause ensures that customers do not remain with a trader whose agreement has been terminated. This provides for a more efficient market.

The draft DDA contains provisions that set out the events to occur on termination. Unison's agreement has an additional action that states that:

> *21.6(c)until such time as the Electricity Authority introduces a default retailer provision, the Distributor may notify any Consumer that there is no longer a use of system agreement between the Retailer and the Distributor and the Consumer needs to enter into a Consumer Contract with an electricity retailer who does have a current use of system agreement with the Distributor, provided that the information contained in that notice is not inaccurate or misleading.*

Unison takes it upon itself to notify customers to seek an agreement with another retailer. This provides customers with information about the status of their retailer and that they need to seek a new retailer. It increases efficiency in the market by ensuring that customers have a retailer and will be paying for their electricity use. It also enhances competition by letting customers know that they need to contract with a new retailer.

3.2.9 Electricity Information Exchange Protocols

Customer information provisions are set out in clause 31.2 of the draft DDA which state that the Trader must on reasonable written request from the Distributor, and within a

reasonable timeframe, provide the Distributor with such Customer information as is reasonably available to the Trader and necessary to enable the Distributor to fulfil its obligations in accordance with this Agreement etc.

Vector's agreement includes a clause 29.3 *Consumer information received in error by Retailer: The Retailer undertakes and agrees that in the event that it or anyone acting on its behalf receives any information relating to consumers on the Network directly or indirectly from the Distributor that does not relate to Consumers the Retailer is supplying at that time, it will keep such information confidential and will not use that information for any purpose. The Retailer acknowledges and agrees that this clause 29.3 shall also be for the benefit of other retailers and enforceable by each of those retailers in accordance with section 4 of the Contracts (Privity) Act 1982.*

The Vector clause protects customer information received in error. It affects competition (information about customers) and efficiency (cost of dealing with the error will be lower than not having such as process). The addition of the clause to the DDA would be beneficial to competition in the industry.

3.2.10 Privacy of service interruption information

Under draft DDA clause 4.2 the distributor may publish or disclose any information relating to any Service Interruption. Vector's agreement is consistent but in addition specifies that:

> *In disclosing such information, the Distributor will comply with its obligations under the Privacy Act 1993".*

The Privacy Act controls how *agencies* collect, use, disclose, store and give access to *personal information*.[2] Vector's addition enhances the interest of consumers by ensuring that the Distributor complies with privacy legislation if it decides to release any information on Service Interruption.

3.3 Reliability

In its Consultation Paper the EA states that the proposal is not expected to affect the reliability of supply of electricity.

We consider that there are a number of areas where the EA's proposal will affect reliability.

3.3.1 Good Electricity Industry Practice

Currently in the general obligations, Clause 2.1 of the draft DDA sets out that that Purpose of the clause is intended to provide an overview of each party's obligations under this Agreement, and does not impose any legal obligations on either party.

In the comparable clauses in both Unison and Vector negotiated contracts (clauses 2.1 and 2.2), the services and obligations of the trader and distributor are framed with reference to Good Electricity Industry Practice:

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2 As viewed at https://www.privacy.org.nz/the-privacy-act-and-codes/privacy-act-and-codes-introduction

2.1 Distributor's services and obligations: Subject to the terms and conditions of this agreement, the Distributor will in accordance with Good Electricity Industry Practice…

2.2 Retailer's services and obligations Subject to the terms and conditions of this agreement, the Retailer will in accordance with Good Electricity Industry Practice…

The reference to Good Electricity Industry Practice in the listing of services and obligations provides a comprehensive cover for all the services and obligations. GEIP is a well-known and defined term. The concern is that removing this term creates uncertainty about the boundaries to the standards and the extent of liability.

The uncertainty about the impact on liability is increased with the replacement of the use of 'will' to the form of 'must' throughout the draft DDA. The use of the term 'must' places a more onerous obligation on the party to act.

3.3.2 System Emergency Event Management policy

Draft DDA clause 4.3 strengthens the requirement on Distributors to have a System Emergency Event management policy and to manage System Emergency Events in accordance with the Emergency Event Management Policy. The policy is to be set out in Schedule 4 of the DDA template and is an operational term.

The new clause replaces the MUoSA clause and removes reference to the policy having to be consistent with Good Electricity Industry Practice but that the distributor will not be in breach of the policy if it has acted in good faith.

Vector's agreement requires it to have a protocol on the priorities for Load Shedding and that the protocol is Confidential Information under the agreement (VUoSA clause 5.3).

The requirement to have a System Emergency Event Management Policy and to manage System Emergency Events accordingly enhances reliability. However it would be more appropriate and promote better outcomes to retain reference in the DDA to the policy being consistent with Good Electricity Industry Practice.

It would also be preferable to ensure that the distributor will not be in breach of the policy if it has acted in good faith.

The reference to Good Electricity Industry Practice and acting in good faith may be covered in the operational terms but it would be beneficial to have it standardised in the DDA to ensure consistency across the industry. Good Electricity Industry Practice is a defined and well-understood term which underpins industry standards and operations. Distributors should also be able to have the ability to ensure that the System Emergency Event management policy is treated as Confidential Information. It is likely that at least some aspects of such a policy may not be beneficial if made publicly available – for example, the order in which load is managed in an emergency event.

3.3.3 Customer request for restoration of Distribution Services

Under draft DDA clause 4.7 during any Unplanned Service Interruption, unless the Distributor requests otherwise, the Trader must forward to the Distributor any requests it receives from Customers for the restoration of the Distribution Services as soon as

practicable, and the Distributor must acknowledge such receipt unless the Trader requests otherwise. Unison and Vector's agreements do not require the Distributor to acknowledge such receipt.

The draft DDA places a stronger obligation on the Distributor to acknowledge receipt of customer requests for restoration of Distribution Services.

The potential benefit of this clause is that traders will be able to inform customers that their requests have been acknowledged by the distributor. This is beneficial for customers.

We understand some distributors have systems in place to meet this requirement. Distributors who do not are likely to face higher costs to meet this obligation.

The draft DDA clause may provide better information to customers but it will come at a cost to distributors which will be passed on to customers.

3.3.4 Complying with communication policies

The Distributor must comply with the requirements set out in Schedule 5 in relation to the notification of Planned Service Interruptions (draft DDA clause 4.9). WEL's agreement is consistent but also places an obligation on the Trader (Retailer) to comply with Schedule 5. If the Trader does have obligations in relation to the notification of Planned Service Interruptions, then the WEL clause provides greater certainty and clear accountability and is preferable to the draft DDA clause.

3.3.5 Trader to control load

Provisions for the trader to control load are set out in clause 5.2 of the draft DDA. Vector's agreement is consistent with this provision but adds the requirement for the Trader to enter into an agreement that sets out a protocol.

VUoSA 6.2 ***Retailer may control load**: […]. Prior to operating its Load Control System, the Retailer will enter into an agreement with the Distributor which sets out the protocols for the use of the load, including the co-ordination with the Distributor of the disconnection and reconnection of load, such protocols being intended to ensure that the security, safety and integrity of the Network is not adversely affected by such load control. The Distributor will consult with the Retailer for a reasonable period (which may be undertaken jointly with other retailers) in relation to such protocols, and the parties will act in good faith in negotiating and seeking to agree the same. If the parties cannot agree such protocols within 40 Working Days, then either party may raise a Dispute to be determined in accordance with the Dispute resolution process in clause 25. The Retailer shall ensure that such protocols are followed when operating its Load Control System. Without limiting the foregoing, the Retailer will ensure that it does not operate its Load Control System in a manner that it knows will or may adversely affect the security, safety or integrity of the Network.*

This requirement enhances reliability. It provides a way of setting out the manner in which load that is managed by a trader will be used and managed; seeking to ensure security, safety and integrity of the Network; and proving a process for dispute resolution.

We note that Clause 5.6 of the draft DDA sets out a prescriptive approach for the trader to make controllable load available to the Distributor for management of system security. A protocol could cover other matters.

The requirement to have an agreement or protocol should be added to core terms of the DDA. The actual protocol could be set out in Schedule 8 and should be made publicly available.

3.3.6 Access to customer's premises

Clause 11 of the draft DDA contains the provisions for access by a Distributor to a customer's premises. Vector's agreement includes and additional provisions (h) *for any other purpose related to the provision of Services under this agreement or to enable the Distributor to comply with law.*

This additional wording provides a more comprehensive coverage of the distributor's right to access premises if it needs to comply with the clause. It removes any ambiguity about the distributor's ability to do so. This clause enhances reliability relative to the draft DDA.

3.3.7 Notification of interference, damage or theft

Under the draft DDA (clause 12.9) both the trader and distributor have obligations to notify the affected party if they discover any interference or damage to the other party's equipment or the Customer's Installation, or evidence of theft of electricity, loss of electricity or interference with the Network.

Vector's agreement adds an obligation on the trader to *notify the Distributor of any other incident or matter that the Retailer has actual knowledge of, or that the Retailer ought to have knowledge of acting in accordance with Good Electricity Industry Practice, which could have an adverse effect on the Network or the supply of electricity to or from the Network.*

This obligation is consistent with the Vector approach to link obligations to Good Electricity Industry Practice which provides a framework for obligations on the distributor and trader. In this case it provides a consistent framework for obligations on the trader. The obligation is focused on 'adverse effects' on the Network or the supply of electricity to or from the Network which improves obligations relating to reliability and security of the network compared to the draft DDA.

3.3.8 Further indemnity

Clause 27 of the draft DDA lists the circumstances when a distributor will be indemnified by the trader. In relation to clause 27.1(a) (ii) Vector's agreement has an additional sentence that does not indemnify the distributor where the distributor has not acted in accordance with Good Electricity Industry Practice.

> *VUoSA 26.15(a) (ii)the disconnection by the Retailer, or disconnection requested by the Retailer, of any Consumer's Premises in accordance with this agreement except where the disconnection is effected by the Distributor and is not undertaken in accordance with Good Electricity Industry Practice;* (emphasis added)

This obligation is reciprocated for traders being indemnified by distributors. (Draft DDA clause 27.2(a) (ii)

This clause provides greater protection to the trader and is preferable to the draft DDA.

3.4 Efficiency

The Electricity Authority in its Consultation Paper expresses particular concern with transaction costs stating that:

> *The more difficult or costly it is for a retailer and distributor to negotiate and agree a UoSA, the more it costs for those parties to do business. Those costs are reflected in the costs passed on to a consumer by the consumer's retailer. The costs of agreeing a UoSA may also discourage a retailer from trading on a network. Consumers are affected if there is less retailer choice on a network.*

3.4.1 Cost of doing business

This is a valid concern, but it is not clear whether the Electricity Authority's proposed approach will achieve a reduction in the costs of doing business for either retailers or distributors.

The main reasons are that:

- The draft DDA covers Distribution Services (Introduction). Retailers and distributors will be required to negotiate additional agreements for non-distribution services. This introduces a number of costs and risks, which ultimately are passed onto customers.
- The consultation paper states that its proposal does not affect additional services (i.e. non-distribution services); additional services can still be agreed between traders and distributors and existing agreements for additional services are not affected.[3]

It is not clear what the Electricity Authority means by its statement given that the intention is for the DDA to replace negotiated agreements.

The exclusion of all services other than Distribution Services from the agreement between traders and distributors is a radically different approach to the one that has developed under the current arrangements.

Under the current arrangements traders and distributors can voluntarily include other services providing a comprehensive application of services and obligations tailored to the requirements of the individual businesses and operational functionality. There is a risk that multiple contracts may be disjointed and more difficult for both traders and distributors to manage multiple operational requirements. Examples include arrangements with embedded generators.

We understand from distributors that around 15 services are excluded from the draft DDA. Parties will require different contracts for other services. Reducing the scope of the contracts will result in duplication of effort and higher costs for contracting parties.

Other distributors such as Vector, which is owned by the Auckland Energy Consumer Trust, includes in its negotiated agreement a requirement for retailers to provide information services for it to maintain an accurate register of beneficiaries, to meet its obligations under the trust deed.

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[3] Electricity Authority 2016, Consultation Paper, para. 3.3.24.

It is difficult to see how requiring distributors to contract separately for non-distribution services will reduce the current economies of scale and scope under the current arrangements.

Noting the comments made by the EA in its Consultation Paper, we suggest that other distribution services should be allowed to be included in operational terms. This will avoid an increase in transaction costs resulting from implementing the mandated DDA.

3.4.2 Schedule Planned Service Interruptions

The draft DDA requires that the Distributor must, as far as is reasonably practicable, schedule Planned Service Interruptions to minimise disruption to customers. Vector's agreement is consistent but adds the additional requirement for the Distributor to schedule planned interruptions in "a safe and efficient manner" (VUoSA clause 5.8).

A greater emphasis on safety and efficiency (reducing cost) is beneficial to customers.

3.4.3 Restoration of Distribution Services

In clauses 4.10(a) and (b) of the draft DDA, the term "as soon as practicable" has been replaced with "as soon as possible" with regards to restoring Distribution Services for Unplanned Service Interruptions and Planned Service Interruptions and no later than the timeframes in Schedule 1.

The term "as soon as possible" is not as appropriate as "as soon as reasonably practicable", which is a more common term and more widely understood than the DDA wording. "As soon as possible" implies that the restoration should be undertaken at any cost. This could lead to restoration costs that are higher than necessary. In any case, restoration timeframes are to be set out in Schedule 1.

3.4.4 Distributor may control load

Clause 5.1 of the draft DDA states that *If the Distributor provides a Price Category or Price Option that provides for a non-continuous level of service by allowing the Distributor to control part or all of the Customer's load (a "Controlled Load Option"), and the Customer elects to take up the Trader's corresponding price option that incorporates the Controlled Load Option, the Distributor may control the relevant part of the Customer's load in accordance with this clause. Xx. Schedule 1 and Schedule 8.*

In some cases distributors do not have price categories or price options as set out in draft DDA clause 5.1, but do send ripple and other signals which support customer response to dynamic peak pricing signals.

The ability for distributors to control load in this dynamic way improves the operational efficiency of the network (and potentially the reliability). The draft DDA could be improved by making it clear that ensuring that this type of dynamic load management was not precluded from occurring under the DDA.

If this type of load management was not allowed it would result in reduced efficiency by way of network utilisation.

3.4.5 Indemnity related to control load by trader

In relation to the load management (clause 5 in the draft DDA), WEL's agreement includes the provision to indemnify the Distributor as follows:

WUoSA clause 6.6(e) indemnify and hold harmless the Distributor if the control of all or any part of a Consumer's load by the Retailer results in the Distributor incurring any costs, loss, claim or liability that the Distributor would not have incurred if that load had been controlled by the Distributor.

This provides a strong incentive for the trader to ensure that it does not cause any costs, loss, claim or liability to the Distributor as a result of its load control activities. The WEL clause enhances the existing indemnity provisions in the draft DDA.

3.4.6 Distributor to investigate adverse trends in Losses

The draft DDA places an obligation on the distributor to investigate adverse trends in losses: *If over time Losses trend abnormally away from expected or historical Losses, the Distributor must use reasonable endeavours to identify the cause of the abnormal movement. If the Distributor is unable to identify the cause of the abnormal movement, the Distributor must provide relevant information to all affected traders and must, if requested by the Trader, facilitate a meeting of all affected traders to attempt to resolve the matter.*

It may be more appropriate to require the distributor to investigate losses in accordance with Good Electricity Industry Practice as for traders in clause 6.5 (**Non-technical Losses**: The Trader must investigate and minimise, in accordance with Good Electricity Industry Practice, non-technical Losses).

3.4.7 Pricing Methodology

As discussed in section 3.1.3, the definition of Pricing Methodology referred to in draft DDA clause 7 is unclear. Pricing methodology implies a broader range of matters compared to pricing structures, such as cost allocation between pricing categories.

As such this is likely to have implications on the costs incurred by distributors to consult on changes to prices as required under the draft DDA (clause 7.4).

3.4.8 Price changes

Provisions in the draft DDA (clause 7.2) limit price changes to not more than once in any period of 12 consecutive months to a limited number of situations. The agreements by Vector and WEL add further uncontrollable costs to this list.

WEL's agreement adds:

- *or any mandatory rules or mandatory protocols of any industry association or body to which both the Distributor and the Retailer are members of or signatories to* and
- *any charges imposed by the System Operator or a Local Network Owner;*

Vector's agreement adds:

- *any determination, direction or decision of a regulatory agency.*

The Vector and WEL clauses are more comprehensive and would remove any uncertainty about the status of cost increases that were based on uncontrollable costs.

3.4.9 Changes containing an error

Provisions relating to changes containing an error (draft DDA Clause 7.7) could be improved.

Vector's agreement refers to the trader finding an "arithmetic error". Vector's clause provides obligations on the distributor to provide 40 days' notice and limits the consultation to the error. This is a more efficient process than the MUoSA/DDA.

3.4.10 Trader may request allocation of an alternative eligible Price Category to an ICP

Clause 8.2 of the draft DDA, allows a Trader at any time to request that the Distributor allocate an alternative Price Category to an ICP.

There is a concern that the ability to request changes to the Price Category at any time will lead to traders seeking to change price bands on a seasonal basis (as a customer load profile changes). This could affect the distributor's ability to recoup costs as prices are set annually.

Vector's agreement allows the trader to request that the distributor allocate an alternative Price Category to an ICP at any time, but no more than once a year (unless supply at the ICP has changed to a new Consumer). This is a preferable provision as it prevents "seasonal arbitrage" by traders.

3.4.11 Billing information and payment

Clause 9.1 of the draft DDA requires the trader to provide information to enable the Distributor to calculate Distribution Services charges and prepare Tax Invoices, in accordance with Schedule 2.

In some cases however, the Distributor may prefer to use their own information.

As such, WEL's agreement contains the clause that (b) *The Distributor may elect, by notice to the Retailer, to use its own information to calculate all or part of the Distribution Services charges payable by the Retailer in accordance with this clause 11.*

Similarly Vector's negotiated agreement provides for a pro forma tax invoice to be issued prior to the actual, which is the billing approach for Vector's Northern network and the preferred billing method for some retailers on Vector's Auckland network. It would be preferable for the DDA to allow Distributors and Traders to continue their mutually agreed billing approaches, and in any case continue to use their own information and/or estimates having given the trader notice. This avoids having to "wait and see" if the retailer provides its data on time before estimating the tax invoice. In some cases, the ability for the distributor to estimate the invoice may be more timely and efficient.

3.4.12 Additional security requirements

Distributors may require traders to provide additional security requirements (draft DDA clause 10.10) which is limited to the Distributor's reasonable estimate of the charges that the

Trader will be required to pay to the Distributor under this Agreement in respect of any two month period.

An alternative and more flexible approach is provided in Vector's Clause 12.7. Where a retailer has opted to provide a level of security greater than the Additional Security required by the distributor, Vector's UoSA allows for parties to mutually agree that the distributor will hold the excess security but will not be required to pay interest on the excess (i.e. the amount above what is required). In effect, the trader is providing a larger facility that adjusts as the trader's market share grows, reducing the burden and transaction costs on retailers that would otherwise have to continually seek to negotiate additional security from security providers. This reduces transaction costs for the trader and offers a more efficient approach, especially for traders that are growing quickly.

Vector's negotiated UoSA provides added efficiency and is a benefit to traders who are growing their market share.

3.4.13 Interference or damage to Distributor's equipment by Customers

The draft DDA sets out the traders' obligations to include in its connection agreements with customers that the customer must not interfere with or damage the distributor's equipment. Vector's agreement includes an additional requirement to allow the distributor to recover its equipment prior to destruction of the Customer's Premises.

Refer to VUoSA clause 14.1(d*)* *will provide the Distributor with a reasonable opportunity to recover the Distributor's Equipment prior to any destruction of the Consumer's Premises.*

Vector's additional clause is more comprehensive and provides certainty that the equipment can be recovered. This allows the distributor to recover equipment that could potentially be installed at another premise. Therefore the Vector clause reduces waste and enhances productive/technical efficiency.

3.4.14 Force majeure

Force majeure events are defined in clause 21.1 of the draft DDA. Clause 21.1(c) has been amended to make reference to Good Electricity Industry Practice so that a Force Majeure Event occurs if: *the failure did not occur because the party invoking this clause failed to act in accordance with Good Electricity Industry Practice. That is, even if the party acted in accordance with Good Electricity Industry Practice – it can be force majeure.*

This is based on clause 21 of the Vector agreement.

One variation between the draft DDA and the negotiated agreements relates to clause 21.1(b) (i) (B) *A Force Majeure Event occurs if: such failure is caused by: any event or circumstance occasioned by, or in consequence of, any act of God, being an event or circumstance that could not have reasonably been foreseen or, if foreseen, could not reasonably have been resisted;*

Vector's contract has an additional clause:

> *VUoSA 23.1(b)(i)(C) if it was reasonably foreseeable, the failure did not occur as a result of the party invoking this clause 23 failing to act in accordance with Good Electricity Industry Practice; or*

Vector's clause recognises the price/quality trade-off that occurs in managing foreseeable events on a network. It is a more comprehensive description of what is excluded from Force Majeure. The reference to Good Electricity Industry Practice is preferable as it puts a framework around the cost of managing the network. Without the reference to Good Electricity Industry Practice there is uncertainty about the appropriate parameters for managing reasonably foreseeable events.

In turn the open-ended draft DDA potentially leaves the distributors open to greater exposure to liability for negligence.

In addition, the draft DDA clause 21.1(b) (v) refers to *A Force Majeure Event occurs if: such failure is caused by any other event or circumstance beyond the control of the party invoking this clause 21.1* (emphasis added). Vector's agreement uses the term "reasonable control" which is preferable to limit the expectations of what the party can control. In this circumstance, the ability to control can be influenced by several factors – but they may not be reasonable.

3.4.15 Charges continue if a Force Majeure Event occurs

Unison and Vector agreements contain clauses clarifying that fixed distribution charges continue if a Force Majeure Event occurs. For example Unison's UOSA clause 23.6:

> *(a) the occurrence of such Force Majeure Event will not affect the parties' obligations in relation to the calculation and payment of fixed charges in relation to the Services (whether or not, in the case of charges relating to ICPs, the relevant ICP received a supply of electricity during the period of the Force Majeure Event); but*
>
> *(b) any variable charges applicable to ICPs will not be payable to the extent that the consumption of, or demand for, electricity at the ICP is reduced due to the Force Majeure Event; provided that where access to any Consumer's Premises is prevented by law or a regulatory authority, other than due to any action or inaction on the part of the relevant Consumer, fixed charges will not be payable during which such access is prevented.*

This clause recognises that charges still need to be paid because the restoration of services after a Force Majeure Event is a Distribution Service. It fits within the definition of "*the provision, maintenance and operation of the Network for the conveyance of electricity to Customers.*" It ensures that customers are contributing to the restoration of services and that the distributor is not disadvantaged by loss of revenue for an event that was not within its control.

Unison's clause provides that customers who are prevented by law or regulatory authority from accessing their premises will not pay fixed charges. This seems to be a reasonably equitable and balanced approach that benefits customers who are prevented from accessing their premises.

3.4.16 Court proceedings

In relation to dispute resolution procedures, the draft DDA contains a provision (Clause 23.10) that allows either party to initiate court proceedings in relation to the Dispute.

The negotiated agreements do not have this clause. The draft DDA is preferable because it provides an incentive for the parties to resolve their dispute otherwise Court proceedings which are more costly and onerous on the parties could be initiated.

3.4.17 Limitation of liability

Clause 24.6 states that *the maximum total liability of each party to the DDA (whether in contract, tort (including negligence) or otherwise) for any single event or series of connected events will not in any circumstances exceed the lesser of $10,000 for each ICP on the Network at which the Trader supplied electricity on the day of the event, or $2,000,000.*

The clause is an attempt to limit the maximum liability of each party. Limiting the liability places a cap on the cost that parties would be expected to incur in contract, tort (including negligence) or otherwise. From an economic perspective this aims to limit the risk and cost of parties to the DDA.

The way the clause is currently drafted however is not an effective means of limiting liability.

The draft DDA provision fails to cap the value of liability that parties would be subject to payout on an annual basis. There is no definition for "single event of series of events". Several "single events" or "series of events" in a year could affect the financial viability of the parties to the agreement. In effect, the draft DDA provision does little to place a limit on potential liability.

Vector's agreement caps the liability to an annual aggregate amount based on market share of the trader. We understand that Orion's agreement has similar provisions. WEL's agreement also places an annual cap on the value of liability. These are more effective provisions for limiting liability and the risk to the industry.

Basing the maximum aggregate liability of the distributor and the trader on the trader's market share on the network is beneficial for retailers. It takes into account the size of the traders' activity on the network and by implication ability to manage the related risk. This type of proportionate cap is beneficial to competition. Another concern is that this clause does not refer to Good Electricity Industry Practice and so potentially reduces the effectiveness of the limitations of liability clause.

Another issue is that there is limited correlation between the event and the parties that are actually affected. The limitation is expressed per ICP on the Network at which the Trader supplied electricity on the day of the event. This implies that the value of the liability depends on how many ICPs are with the trader – rather than how many ICPs are affected.

Vector's agreement deals with this by relating the claim to each ICP on the network in relation to which a claim has been made.

> *VUoSA clause 26.7(a) subject to the further limitation of the maximum total liability of the Distributor to the Retailer in any Year under sub-clause (b), in respect of a single event or series of connected events, not in any circumstances exceed, in respect of each ICP on the Network in relation to which a claim has been made, the lesser of:*
>
> *(i) $10,000, where the relevant ICP is a Residential ICP or $20,000, where the relevant ICP is a Non-Residential ICP; and*
>
> *(ii) the amount of the claimable loss or damage suffered.*

Vector has different values for residential ICPs and non-residential ICPs as well as a further provision limiting the liability to the amount of the claimable loss or damage suffered. This type of clause would prevent nuisance claims.

A provision that better correlated the limitation of liability to affected parties and to the claimable loss or damage suffered is preferable to the uncorrelated provision in the draft DDA. This would limit the cost and improve the technical efficiency in the industry.

3.5 Long term interests of consumers

For the most part our comparison of the variances in draft DDA and the negotiated agreements of Unison, Vector and WEL lead us to conclude that none of the agreements would have a detrimental effect on the statutory objective. In many cases, the negotiated clauses would enhance competition, reliability and/or efficiency.

In our view the Electricity Authority acknowledged that commercial negotiations can lead to better agreements by including clauses from Vector's agreement into the draft DDA. As a result there is substantial alignment between the draft DDA and the negotiated agreements we examined.

Notwithstanding the substantial alignment and immaterial changes in the DDA, there are differences on significant matters such as limits of liability and the application of Good Electricity Industry Practice. Without these significant matters being properly assessed and the apportionment of risk/cost better balanced (i.e. Good Electricity Industry Practice removal and changes to Force Majeure (FM) and liability caps) the DDA will result in an increase in the cost of providing the same level of distribution service.